Supreme Court, U.S.
FILED

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No. _____

In The
Supreme Court of the United States

PIONEER COMMERCIAL
FUNDING CORPORATION,

Petitioner,

V.

CORESTATES BANK, N.A.

On Petition For A Writ Of Certiorari
To The Pennsylvania Supreme Court

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the Pennsylvania Supreme Court deprived petitioner of the process due under the Fifth and Fourteenth Amendments when it reversed the decision of the Pennsylvania Superior Court in petitioner's favor by making *de novo* factual findings, contrary to the findings of the jury and trial court, notwithstanding the promise of a right to trial by jury in the Pennsylvania Constitution, without giving petitioner fair notice of the questions on the basis of which the appeal would be decided.

PARTIES TO THE PROCEEDING

Petitioner is a publicly traded company, but there is no parent corporation or publicly held company holding more than 10% of Pioneer's stock.

The respondent is CoreStates Bank, N.A. American Financial Mortgage Corporation, Thomas F. Flatley, and Norwest Funding, Inc. were parties to the litigation in the court below but we believe that they have no interest in the outcome of this proceeding.

TABLE OF CONTENTS

	Page
Opinions Below	1
Jurisdiction	1
Constitutional Provisions Involved	1
Statement of the Case	2
Reasons for Granting the Petition	9
Conclusion	24
Appendix	App. 1

TABLE OF AUTHORITIES

Page

CASES:

Anderson v. City of Bessemer City, 470 U.S. 564 (1985) 12

BMW of N. Am., Inc. v. Gore, 517 U.S. 559 (1996) 10

Brinkerhoff-Faris Trust & Sav. Co. v. Hill, 281 U.S. 673 (1930) 20, 21, 22

Carducci v. Regan, 714 F.2d 171 (D.C. Cir. 1983) 19

Cent. Bank v. First Interstate Bank, 511 U.S. 164 (1994) 19

Cooper Indus., Inc. v. Leatherman Tool Group, Inc., 532 U.S. 424 (2001) 10

Griffin v. Illinois, 351 U.S. 12 (1956) 12

Johnson v. New York, N.H. & H.R. Co., 344 U.S. 48 (1952) 12

Lachance v. Erickson, 522 U.S. 262 (1998) 18

Landgrave v. USI Film Prods., 511 U.S. 244 (1994) 21

LeTulle v. Scofield, 308 U.S. 415 (1940) 10

Libengood v. Pa. R.R. Co., 55 A.2d 756 (1947) 11

Lindsey v. Normet, 405 U.S. 56 (1972) 12

McDevitt v. Hutchinson, 119 A.2d 289 (Pa. 1956) 11

Mitzelfelt v. Kamrin, 584 A.2d 888 (Pa. 1990) 11

Moore v. Dempsey, 261 U.S. 86 (1923) 9

Richards v. Jefferson County, Alabama, 517 U.S. 793 (1996) 18

Satterwhite v. Nat'l Powder Co., 66 A.2d 278 (Pa. 1949) 11

TABLE OF AUTHORITIES – Continued

Page

Saunders v. Shaw, 244 U.S. 317 (1917) 18

State Farm Mut. Auto Ins. Co. v. Campbell, 538 U.S. 408 (2003) 10

Walker v. Sauvinet, 92 U.S. 90 (1875) 12

Ward v. Bd. of County Comm'rs, 253 U.S. 17 (1920) 21

Windsor v. McVeigh, 93 U.S. 274 (1876) 18

Zauderer v. Office of Disciplinary Counsel, 471 U.S. 626 (1985) 21

CONSTITUTION

U.S. CONST. amend. V 1

U.S. CONST. amend. XIV, § 1 2

PA. CONST. art. I, § 6 11

STATUTE:

28 U.S.C. § 1257(a) 1

LAW REVIEWS AND TREATISES:

Note, *Appellate Sua-Sponte Activity: Remaking Disputes and the Rule of Non-Intervention*, 40 S. CAL. L. REV. 352 (1967) 20

HENRY J. BAILEY, III & RICHARD B. HAGEDORN, BRADY ON BANK CHECKS: THE LAW OF BANK CHECKS ¶ 15.16[1] 24

BARKLEY CLARK & BARBARA CLARK, THE LAW OF SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE ¶ 3.11[3] (Dec. 2004 update) 24

TABLE OF AUTHORITIES – Continued

Page

BARKLEY CLARK & BARBARA CLARK, THE LAW OF BANK DEPOSITS, COLLECTIONS AND CREDIT CARDS ¶ 17.06[2] (Dec. 2004 update) 24

Barkley Clark & Barbara Clark, *Bank Has Broad Right to Exercise Setoff Against Funds Wired into Beneficiary's Account*, 09-04 CLARK'S BANK DEPOSIT & PAYMENTS MONTHLY (Sept. 2004) 24

OLIVER WENDELL HOLMES, *Law and the Court, in* COLLECTED LEGAL PAPERS 291 (1952) 9

John Leubsdorf, *Constitutional Civil Procedure*, 63 TEX. L. REV. 579 (1984) 9

Robert J. Martineau, *Considering New Issues on Appeal: The General Rule and the Gorilla Rule*, 40 VAND. L. REV. 1023 (1987) 23

ROBERT J. MARTINEAU, MODERN APPELLATE PRACTICE 41 (1983) 20

Adam A. Milani & Michael R. Smith, *Playing God: A Critical Look at Sua Sponte Decisions by Appellate Courts*, 69 TENN. L. REV. 245 (2002) 19, 22

Barry A. Miller, *Sua Sponte Appellate Rulings: When Courts Deprive Litigants of an Opportunity to be Heard*, 39 SAN DIEGO L. REV. 1253 (2002) ... 19, 22, 23

Martin H. Redish & Lawrence C. Marshall, *Adjudicatory Independence and the Values of Procedural Due Process*, 95 YALE L.J. 455 (1986) 9

Richard H. Seamon, *The Sovereign Immunity of States in Their Own Courts*, 37 BRANDEIS L.J. 319 (1998) 22

TABLE OF AUTHORITIES – Continued

Page

Catherine T. Struve, *Direct and Collateral Federal Review of the Adequacy of State Procedural Rules*, 103 COLUM. L. REV. 243 (2003) 20

Stephen C. Veltri, et al., *Payments*, 58 BUS. LAW. 1575 (2003) 24

PETITION FOR WRIT OF CERTIORARI TO THE PENNSYLVANIA SUPREME COURT

Pioneer Commercial Funding Corporation respectfully petitions for a writ of certiorari to review the judgment of the Pennsylvania Supreme Court in this case.

OPINIONS BELOW

The order of the Pennsylvania Supreme Court denying petitioner's application for reargument (App., *infra*, 117) is reported at 864 A.2d 1198. The opinion of the Pennsylvania Supreme Court (App., *infra*, 1-28) is reported at 855 A.2d 818. The opinion of the Pennsylvania Superior Court (App., *infra* 31-68) is reported at 797 A.2d 269. The opinion of the Pennsylvania Court of Common Pleas (App., *infra*, 69-116) is reported at 50 Pa. D. & C. 4th 31.

JURISDICTION

The judgment of the Pennsylvania Supreme Court was entered on December 20, 2004. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(a).

CONSTITUTIONAL PROVISIONS INVOLVED

The Fifth Amendment to the United States Constitution provides, in relevant part: "No person shall * * * be deprived of life, liberty, or property, without due process of law."

Section 1 of the Fourteenth Amendment to the United States Constitution provides, in relevant part: "No state shall * * * deprive any person of life, liberty, or property, without due process of law."

STATEMENT OF THE CASE

Although this case has its roots in a garden-variety commercial dispute between financial institutions, the disposition of the case by the Pennsylvania Supreme Court presents fundamental questions of fairness in the appellate process that command the attention of this Court.

1. The case arises out of a transaction in which petitioner Pioneer Commercial Funding Corporation sold its interest in a package of home mortgage loans to Norwest Funding, Inc. ("Norwest"). To understand that transaction, some background is necessary. At the time of the transactions out of which this litigation arose, petitioner was a "warehouse lender" in California. In that capacity, petitioner served as an intermediary. Thus, it borrowed money from larger financial institutions (specifically Bank One Texas, N.A. ("Bank One")) and then advanced that money to smaller companies that made ("originated") mortgage loans directly to home buyers. Petitioner and its customers recouped their investments by selling the loans to third party investors in the secondary market. In the ordinary process, the promissory notes evidencing the payment obligation would be sent from the originator to petitioner, which in turn would deliver them to Bank One as collateral for Bank One's loan to petitioner. When the loans were sold in the secondary market, Bank One would

deliver the promissory notes to the investor that purchased them. App., *infra*, 2-3, 32-33.

The transaction out of which this case arises involved loans originated in California by a client of petitioner's named RNG Mortgage Services, Inc. ("RNG"). In August of 1997, RNG filed a petition for bankruptcy relief under Chapter 11 of the United States Bankruptcy Code. Although that filing impaired RNG's ability to attract investors in its loans, it did not affect the network of contacts that brought home buyers to RNG. Interested in RNG's underlying pipeline of home buyers, another mortgage originator named American Financial Mortgage Corporation ("AFMC") and its principal (Thomas F. Flatley ("Flatley")) began negotiations to acquire RNG. App., *infra*, 3-4, 32-33.

To maintain RNG as an ongoing business during the course of those negotiations, the affected parties needed to obtain a secondary market investor that would continue to purchase loans originated by RNG despite RNG's bankruptcy filing. The parties quickly settled on Norwest, which already had an existing business relationship with AFMC. RNG's bankruptcy filing was a central problem for Norwest in purchasing loans originated by RNG. Among other things, a typical originator would guarantee that the home buyers actually would fulfill their obligations on the purchased notes, but RNG's bankruptcy made its commitment on that point unreliable. To solve that problem, the parties developed an arrangement in which the notes to be purchased by Norwest would be sent from Bank One to AFMC. AFMC would indorse the notes, accepting secondary responsibility for the obligation of the home buyers to repay those notes, and then forward them to Norwest. App., *infra*, 4-5, 32-34.

The parties used that arrangement to sell two separate portfolios of mortgage loans. The first transaction took place in late October of 1997. Bank One collected the relevant notes and sent them to AFMC. To protect its interest in the notes, Bank One sent the notes along with a so-called "bailee letter," a document widely used in the mortgage industry, which generally states that neither AFMC nor any other party could obtain any interest in the notes until Bank One and petitioner had been paid for them. AFMC indorsed the notes and forwarded them and the bailee letter to Norwest. Norwest wired payment for the portfolio to AFMC's account at respondent CoreStates Bank, N.A., contrary to the wiring instructions in the bailee letter. Pioneer and Bank One were concerned about AFMC having access to the funds for sale of the portfolio. Accordingly, petitioner, RNG, and AFMC jointly contacted Norwest and asked it to send funds for future transactions directly to petitioner's account at Bank One. App., *infra*, 5-6, 33-34.

The second transaction occurred in November 1997. As in the first transaction, Bank One transmitted the documents to AFMC under cover of a bailee letter specifying that no party could obtain an interest in the loans until Bank One received payment for them; the letter identified a particular account of petitioner's at Bank One to which payment was to be made. Among other things, the bailee letter stated:

> The Collateral is being delivered to you for purchase under the existing Take Out Commitment [issued by Norwest]. * * * Either payment in full for the Collateral or the Collateral itself must be received by Agent within 45 days after the date of this letter. Unitl [sic] that time, you are

> deemed to be holding the Collateral in trust, subject to the security interests [held by Bank One and Pioneer].

App., *infra*, 118. Despite the wiring instructions and the bailee letter, apparently in response to a request from AFMC, Norwest sent funds for that transaction (about $1.7 million) to AFMC's settlement account at respondent. Unfortunately for all involved, the situation quickly unraveled from that point. By the date of that wire transfer, respondent had reacted to a long-standing pattern of check-kiting by AFMC by placing a restraint on AFMC's account. Although AFMC promptly submitted a letter to respondent formally disclaiming any interest in the funds, respondent refused to release the funds. App., *infra*, 124. Several months later, respondent offset the funds in the account against AFMC's outstanding obligations to respondent. In part because petitioner was a highly leveraged firm, and in part because of uncertainty about its operations because of this dispute, petitioner's operations steadily contracted; petitioner ceased business as an operating company in the summer of 1999. App., *infra*, 5-9, 33-36.

2. Unable to persuade respondent to release the funds voluntarily, petitioner instituted this litigation in the Pennsylvania Court of Common Pleas. The central issue at trial was the nature of the transmission from Bank One to AFMC. Petitioner contended that the transactions reflected a sale from RNG and petitioner, on the one hand, to Norwest, on the other, and that the bailee letter prevented AFMC from obtaining any interest in the documents. AFMC's role was solely to provide a secondary assurance of the reliability of the loans. From that perspective, it seemed tortious for respondent to retain funds

sent to AFMC as payment for petitioner's property. Respondent, on the other hand, contended that the transmission from Bank One to AFMC reflected a sale of the documents to AFMC, followed by a transfer of the documents to Norwest. From that perspective, respondent argued, it was permissible for respondent to retain funds wired to respondent as payment for assets sold by AFMC. After an extended and contentious trial, a jury ruled in favor of petitioner and awarded compensatory damages of about $15 million, together with punitive damages of $337.5 million. In response to post-trial motions, the trial court upheld the award of compensatory damages, but reduced the punitive damages award to $40.5 million. App., *infra*, 11-13, 36-37, 101-105.

3. Respondent appealed to the Pennsylvania Superior Court. Because the trial court's decision rested in part on the view that it is permissible to sue a bank for conversion of funds sent by wire transfers, the Federal Reserve Banks filed a joint amicus brief in support of respondent, urging reversal of the decision of the trial court. In March 2002, the Superior Court affirmed the judgment in favor of petitioner, but overturned the amount of the punitive damages, remanding the case for a retrial on the amount of punitive damages. App., *infra*, 31-68. Respondent filed an application for reargument and rehearing en banc. In May 2002, that application was denied without opinion; no judge of the Superior Court noted a dissent from that denial.

4. Respondent then sought discretionary review from the Pennsylvania Supreme Court through a petition for allocatur. After a delay of more than a year, that court granted the petition in December 2003, articulating a list of five specific questions on which the parties were to submit briefs and argument. App., *infra*, 29-30.

5. The parties submitted briefs on the questions articulated by the court. The issues on which the court called for briefing included questions of considerable commercial significance – most obviously the question mentioned above, regarding the extent to which a third party that does not participate in a wire transfer can sue a bank for conversion of funds it receives by a wire transfer to one of its customers. Accordingly, the case received considerable attention from amici on both sides. As at the Superior Court stage, the Federal Reserve Banks submitted a brief arguing that the Pennsylvania Supreme Court should overturn the decision of the Superior Court. In April 2004, the Pennsylvania Supreme Court heard oral argument on the questions on which it had sought briefing.

The court resolved the case in an opinion issued in August 2004. That opinion did not resolve any of the five specific questions on which the court had granted review and received oral argument and briefing. On the contrary, the Court resolved the case by determining *de novo* that the factual record did not provide adequate support for the findings of the jury. To justify that judgment, the Court made two related findings.

a. First, it argued that the record compelled the conclusion that when Bank One transmitted the documents to AFMC it was effectively making a loan to AFMC, so that title to the documents passed immediately to AFMC. App., *infra*, 17-21. As should be clear from the discussion above, that finding reflects an understanding of the record not previously supported by either party in the litigation. At trial, the parties had debated whether RNG and Pioneer had sold the documents to AFMC for resale to Norwest or instead had sold them directly to Norwest. Nobody ever had suggested that the transfer to AFMC

reflected a sale on credit to AFMC – largely because there was no document suggesting a lending relationship between Bank One and AFMC and no evidence that AFMC ever agreed to pay anybody for the loans.

b. Second, the court had to reject the significance of the bailee letter. That was more difficult for the court, because it was indisputably the only document that accompanied the transmission from Bank One to AFMC, because it directly and incontrovertibly contradicted the understanding of the transaction on which the court based its judgment, and because it is a common document of great commercial significance. The court expressly acknowledged that the bailee letter was inconsistent with its understanding of the record but still concluded – without identifying any specific evidence in the record, and despite the contrary verdict of the jury – that the record compelled the conclusion that stated that AFMC acquired ownership of the documents it received under cover of the bailee letter.

6. Petitioner submitted a timely application for reargument. Because the court's disposition ignored the specific terms of the bailee letter, and because those documents are of great importance to the banking industry, a number of mortgage lenders filed amicus briefs in support of the application for reargument, generally urging the court to pull back from a decision so disruptive to industry practice. The application for reargument specifically raised the due process questions presented in this petition.

The Pennsylvania Supreme Court denied the application for reargument without opinion on December 20, 2004. App., *infra*, 117.

REASONS FOR GRANTING THE PETITION

In Our Federal system, this Court stands as the only institution that can compel the judiciaries of the States to adhere to the Constitution. Indeed, although this Court reviews judgments of federal courts much more frequently than judgments of state courts, structural principles suggest that vigilance in reviewing the decisions of state courts is more fundamental to the stability of the system. *See* OLIVER WENDELL HOLMES, *Law and the Court*, *in* COLLECTED LEGAL PAPERS 291, 295-96 (1952) ("[T]he Union would be imperiled if we could not make that declaration as to the laws of the several States."); *cf. Moore v. Dempsey*, 261 U.S. 86 (1923) (per Holmes, J.).

The central point of our petition is that the Pennsylvania Supreme Court's decision in this case so departs from traditions of fair notice and an orderly judicial process as to transgress the bounds of the Due Process Clause of the Fourteenth Amendment. We recognize that this Court for many years did not have a robust tradition of policing the manner in which state courts operate their appellate process. *See* John Leubsdorf, *Constitutional Civil Procedure*, 63 TEX. L. REV. 579 (1984) (decrying the Court's reluctance to exercise more scrutiny in this area). More recently, however, the Court has begun to recognize the need for supervision to ensure some minimal level of fairness in civil litigation conducted in state courts.[1] This is seen most plainly in the recent line of cases involving

[1] At least implicitly, the need for review can be related to the tradition of electing judges in most state court systems. *See* Martin H. Redish & Lawrence C. Marshall, *Adjudicatory Independence and the Values of Procedural Due Process*, 95 YALE L.J. 455 (1986) (arguing that the Due Process Clause requires appointment of state court judges).

punitive damages.[2] As those cases suggest, this concern is particularly important in cases that involve litigation between entities firmly situated in the local milieu (like respondent) and out-of-state businesses (like petitioner).[3]

Problems in the civil process are not, however, confined to the determination of damages. Indeed, more than sixty years ago, this Court granted review to consider a question closely related to the question that we present here, the propriety of a decision on a ground not argued by the parties without fair notice to adversely affected parties. *See LeTulle v. Scofield*, 308 U.S. 415, 416 (1940) ("We took this case because the petition for certiorari alleged that the Circuit Court of Appeals had based its decision on a point not presented or argued by the litigants, which the petitioner had never had an opportunity to meet by the production of evidence."). Sooner or later, we submit, this Court will define some minimal appellate process that the Constitution compels. This case offers an excellent vehicle for a first step in that direction, largely because the court in this case went *so far* beyond traditional bounds of decision making that the Court can reverse the judgment in this case without upsetting traditional and customary practices of state courts.

1. a. We start from the point that the articulated law of Pennsylvania, as in all common-law jurisdictions, requires considerable deference to the resolutions of factual disputes by the finder of fact in the trial court,

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[2] *E.g.*, *State Farm Mut. Auto Ins. Co. v. Campbell*, 538 U.S. 408 (2003); *Cooper Indus., Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424 (2001); *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559 (1996).

[3] *Campbell*, 538 U.S. at 420-21; *BMW*, 517 U.S. at 572-73.

particularly when that finder of fact is a jury required by Article I, Section 6 of the Pennsylvania Constitution. As with the Federal judicial process, that provision establishes a process that "vests the responsibility of determining the facts with the jury [so that courts] will not upset their findings absent a showing that the verdict is capricious, against the weight of the evidence and resulted in a miscarriage of justice," *Mitzelfelt v. Kamrin*, 584 A.2d 888, 891 (Pa. 1990). Within that system, there is a standard method in Pennsylvania for evaluating the evidence to support a verdict. Generally, it requires the appellate court to "accept the oral evidence supporting the verdict * * * and reject contrary inferences." *Satterwhite v. Nat'l Powder Co.*, 66 A.2d 278, 280 (Pa. 1949); *see McDevitt v. Hutchinson,* 119 A.2d 289, 290 (Pa. 1956); *Libengood v. Pa. R.R. Co.,* 55 A.2d 756, 757 (Pa. 1947).

As this Court has explained, that tradition is not simply a matter of habit or well-established practice; it is fundamental to sound judicial administration:

> Where there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous. * * * *
>
> The rationale for deference to the original finder of fact is not limited to the superiority of the trial judge's position to make determinations of credibility. The trial judge's major role is the determination of fact, and with experience in fulfilling that role comes expertise. Duplication of the trial judge's efforts in [appellate courts] would very likely contribute only negligibly to the accuracy of fact determination at a huge cost in diversion of judicial resources.

Anderson v. City of Bessemer City, 470 U.S. 564, 573-75 (1985) (brackets, citations, ellipses, and internal quotation marks omitted). Thus, traditional understandings of the right to a jury trial suggest that it offends the right to a jury trial for a court to enter judgment in favor of a party whose submission was rejected by a jury unless the evidence would not permit any reasonable factfinder to reach the conclusion of the jury. *Johnson v. New York, N.H. & H.R. Co.*, 344 U.S. 48, 51-54 (1952).

We do not mean to suggest that a State could not consistently with the Fourteenth Amendment establish a system that dispensed entirely with juries. *See Walker v. Sauvinet*, 92 U.S. 90 (1875). We do think, however, that in a State that has established such a system, the Due Process Clause obligates its appellate judiciary to limit their activities to review rather than *sub rosa* factfinding. *Cf. Lindsey v. Normet*, 405 U.S. 56 (1972) (violation of the Fourteenth Amendment to grant appellate review to some litigants and capriciously deny it to others); *Griffin v. Illinois*, 351 U.S. 12, 20 (1956) (state that provides appellate review for inmates must take steps to make it "adequate and effective").

b. Considered from that perspective, the judgment of the lower court in this case cannot be reconciled with a constitutionally permissible process. Because it rests directly on a *de novo* assessment of a disputed factual record, in a system that promises appellate deference to the resolution of facts by a jury, it has resulted in a deprivation of due process.

Some discussion of the specific factual underpinnings of the lower court's opinion is necessary to illustrate this

problem. We start with the court's conscious decision to reweigh evidence previously considered by the jury:

> We therefore agree with [respondent] that to permit a factfinder to regard the trust proviso of the bailee letter as dispositive would afford too little recognition to the other documents and the overall character of the transaction. We also view the similar characterizations of the transaction by [petitioner]'s lay witnesses at trial as insufficient to overcome the understanding arising from the undisputed structure and purpose of the transaction.[4]

App., *infra*, 22-23.[5]

Analytically, the court's opinion rests on the view that AFMC represented to Norwest that AFMC would have title to the documents, that all of the parties understood AFMC was making those representations, and that

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[4] The clarity of the lower court's foray into post-hoc appellate fact-finding is evidenced not only by the selective reading of the record we discuss in the text, but also by serious errors in the court's understanding of the evidence in the record. Most obviously, the court's opinion at one point draws on the court's interpretation of a zero-balance agreement. App., *infra*, 6 n.10. Because the trial court specifically excluded that agreement from the record, June 28, 2000 tr., pp. 89-93, and that exclusion was not challenged on appeal, the court's reliance on the agreement is indisputably impermissible.

[5] To make the point more clear, the court in a footnote to that passage (App., *infra*, 23 n.30) criticizes petitioner's factual presentation for petitioner's failure to include an expert witness with respect to the "essential distinction between the various commercial relationships." That criticism could be made with equal force about respondent's presentation. In ordinary circumstances, the view of the factfinder that petitioner's presentation was persuasive without such testimony would be more than enough to dispose of that concern, particularly in a case in which respondent did not raise the point on appeal. *See id.* n.30 (emphasizing that "[respondent] does not frame the matter in such terms").

petitioner thus is bound by those representations. The court disingenuously states that its understanding of the transaction is "undisputed" (App., *infra*, 21-23) and consistent "with the knowledge of all concerned" (App., *infra*, 21). At the same time, the court acknowledges (App., *infra*, 23) that petitioner's contrary understanding is supported by the testimony of various officials of both RNG and AFMC.[6]

Moreover, although the court does not acknowledge the point specifically, the court's "undisputed" understanding directly contradicts respondent's own contemporaneous understanding, as evidenced in the internal email on which the trial court and the intermediate appellate court relied. The email indicates that respondent's senior executives, after reviewing the results of a month-long investigation

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[6] For example, a responsible officer of AFMC testified that the loans "were not really considered our loans." Pa. S. Ct. R. 1465a. He went on to explain that the sole reason that AFMC participated in the process was to help RNG get funds to remain in business. *Id.* ("You have to keep in mind, we were just like a vehicle for RNG to pass these loans through to deal with Norwest. * * * * As I said earlier, if you can't sell the loans, you can't turn it in to cash, you can't pay your bills. * * * * And that was what we had to offer help to, to make sure that that happened."). Similarly, a responsible officer of RNG (the originator of the loans) testified that she personally negotiated the purchase prices for the transactions with Norwest, and that AFMC had no role in setting those prices. June 12, 2000 p.m. transcript, p. 61. The relevant executives of AFMC corroborated her testimony on that point. Pa. S. Ct. R. 2170a-2172a (testimony of Joe Scheuren indicating that he listened to the telephone conversations between RNG and Norwest but played no active role). For a more detailed summary of the evidence, *see* petitioner's brief on the merits in the Pennsylvania Supreme Court at p. 4-5 n.3. For present purposes, the key point is that any of that testimony, standing alone, was sufficient to support the jury's verdict. In a jurisdiction that offers litigants the promise of a jury system, the court's dismissal of that testimony does not provide due process.

by its counsel, understood the true structure of the transaction: "This is a payment on a very convoluted transaction involving acompany in bankruptcy in California [RNG] thatsold a portfolio of loans to Norwest. Go Figure how the funds got here." App., *infra*, 123 (punctuation and spelling as in original). Furthermore, the court's repeated suggestions that its opinion implements the "overall" "structure" or "character" of the transaction (App., *infra*, 21-23), are belied by the court's inability to identify any specific document that is unambiguously consistent with the court's understanding. The only document that unambiguously governs the way in which AFMC came to possess the portfolios – the bailee letters – is flatly inconsistent with the court's conclusion.

Turning to the specific factual points that the court articulates, it is plain that the record can not bear the construction that the court places on it. As it happens, much of the most relevant information is not in the reproduced record, which helps explain the court's lack of attention to that material. But that is only because the questions that the court addresses in its opinion are for the most part not the questions on which it requested briefing. Turning to the actual record, the first point of importance is that the record contains no document that directly applies to the subject portfolios in which AFMC warranted to Norwest that it had title to those documents. Indeed, the responsible executive from Norwest testified quite clearly that there was no such representation.[7] There is a general agreement covering transactions that AFMC originated, but the record

[7] July 26, 2000 p.m. transcript, at 92-93 ("Q. * * * Did Mr. Seidman ever represent to you that American Financial had paid for the mortgage loans that would be sold to Norwest? A. No.").

contains nothing to indicate that the document could apply to this transaction originated by RNG.[8]

More fundamentally, neither petitioner nor Bank One knew how AFMC was characterizing the transactions to Norwest. There is a great deal of evidence that Norwest had insisted that AFMC accept responsibility if the underlying homeowners failed to pay.[9] The record makes it clear, however, that Norwest's due diligence investigating AFMC's role did not extend to Bank One or petitioner: neither Bank One nor petitioner had any idea what AFMC was telling Norwest. Rather, to the extent the record discusses the question, it suggests that Norwest's communications about AFMC's role involved inquiries to AFMC and respondent, ***not*** to petitioner, RNG, or Bank One.[10] It is thus insupportable to say, as the court does at App., *infra*, 21, that "the transaction was held out to third parties as a sale with the knowledge of all concerned" or, as the court does at App., *infra*, 23, that the court is implementing "the understanding arising from the undisputed structure and purpose of the transaction."

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[8] Pa. S. Ct. R. 3192a-3193a.

[9] *See* Petitioner's Pa. S. Ct. Br. 3-4. Thus, the court errs when it states at App., *infra*, 21, that the "undisputed objective was to satisfy Norwest's condition that it have a right of recourse against the seller." Norwest's undisputed objective was to have a right of recourse against its customer AFMC. There is nothing to suggest that petitioner, RNG, or Bank One ever were advised that this required making AFMC a formal seller of the documents. That might seem like a small point, but it is the point on which the case turns, a point that the parties debated at considerable length in the trial court, and a point that the jury resolved in petitioner's favor. Fundamental principles of appellate review required the Pennsylvania Supreme Court to defer to the trial court's understanding of that point.

[10] June 27, 2000 tr. 107-08 (testimony of James Lovelace).

In the end, a fair reading of the court's opinion is that it (a) finds incredible all testimony by executives of RNG and petitioner; (b) accepts as credible AFMC testimony that supports respondent and rejects as incredible AFMC testimony that supports petitioner; (c) ignores respondent's internal conclusions that are consistent with petitioner's position; and (d) rejects as irrelevant the only document that directly and indisputably governed the transmission of the notes from Bank One to AFMC – the bailee letter. Without some more explicit justification than appears in the record before this Court, that line of reasoning is irreconcilable with the process that Pennsylvania has promised petitioner, and thus reflects a direct deprivation of the process that is due petitioner under the Fourteenth Amendment.

2. Moreover, because the lower court's procedures and rules led petitioner to limit its presentation in that court to the specific questions written by that court, the court's disposition of the case on the basis of other issues, on which petitioner had no opportunity to be heard, deprived petitioner of due process.

As in most well-ordered courts, the Pennsylvania Supreme Court at every step of its process formally instructed petitioner to refrain from attention by petitioner to questions other than the questions that it formulated for review. App., *infra*, 29-30.[11] The questions on which the court's opinion turns were not included in the questions

[11] We note that the questions formulated by the court are different in important ways from the questions on which respondent sought review, although neither set of questions include the factual and legal issues related to bailee letters that formed the basis of the court's actual decision.

that respondent preserved for appeal from the trial court, were not included in the questions presented in the Bank's petition for allocatur, and were not included in the questions that the court itself drafted to govern the proceedings. Again, on the day of oral argument the court's staff presented petitioner's counsel with the court's "Protocols for Oral Argument," which repeatedly admonish counsel to "avoid a recitation of the facts," and specifically advise appellee's counsel to "respond only to the issues presented by appellant's counsel."[12] Respondent (appellant in the court below) in oral argument did not argue to the court the points on which this case has now been resolved. It was fundamentally unfair for the court to take those actions and then resolve the case as it has, based on a selective reading of the record, with respect to a factual question that was resolved in petitioner's favor at every earlier stage of the proceedings and not fairly included in the questions before the court.

As this Court repeatedly has emphasized, the State does not provide the process that is due when it decides a case without affording a "proper opportunity to present * * * evidence." *Saunders v. Shaw*, 244 U.S. 317, 319 (1917). "The opportunity to be heard is an essential prerequisite of due process of law in judicial proceedings." *Richards v. Jefferson County, Alabama*, 517 U.S. 793, 797 n.4 (1996); *see Lachance v. Erickson*, 522 U.S. 262, 266 (1998) ("The core of due process is the right to notice and a meaningful opportunity to be heard."); *Windsor v. McVeigh*, 93 U.S. 274, 277 (1876) (explaining that an opportunity to be heard "is a principle of natural justice, recognized as

[12] We have lodged a copy of that document with the Clerk. We believe that this Court can take judicial notice of it.

such by the common intelligence and conscience of all nations"). The process of the court below cannot be reconciled with the most basic core of that principle.

Our adversary process rests on the fundamental premise that decisions are best made through the clash of opposing viewpoints. *See Cent. Bank v. First Interstate Bank*, 511 U.S. 164, 195 n.4 (1994) (Stevens, J., dissenting) ("[T]he adversary process functions most effectively when we rely on the initiative of lawyers, rather than the activism of judges, to fashion the questions for review."). Courts "do not sit as self-directed boards of legal inquiry and research," *Carducci v. Regan*, 714 F.2d 171, 177 (D.C. Cir. 1983) (per Scalia, J.). Rather, there are substantial risks of error and procedural unfairness in a process that too readily permits courts to decide questions not presented by the parties.

The specific problem in this case is not a rare or unusual one. On the contrary, academics in recent years have increasingly come to recognize that courts deprive the parties before them of due process when they combine a *sua sponte* decision of points not presented by the parties with a *post hoc* refusal to entertain arguments from the party that is prejudiced.[13] In the decisions of this Court,

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[13] *See* Barry A. Miller, *Sua Sponte Appellate Rulings: When Courts Deprive Litigants of an Opportunity to be Heard*, 39 SAN DIEGO L. REV. 1253, 1260 (2002) ("[S]ua sponte decisions trouble judges because due process interests are implicated when a court recasts the questions presented and decides a case on issues not discussed by the parties without remanding or providing an opportunity for briefing."); Adam A. Milani & Michael R. Smith, *Playing God: A Critical Look at Sua Sponte Decisions by Appellate Courts*, 69 TENN. L. REV. 245 (2002) ("[S]ua sponte decisions by appellate courts * * * are inconsistent with the fundamental principles of due process that a party should have notice of and the opportunity to be heard on the determinative issue in the

(Continued on following page)

the closest parallel to the decision below is the celebrated case of *Brinkerhoff-Faris Trust & Sav. Co. v. Hill*, 281 U.S. 673 (1930). In that case, the Missouri Supreme Court dismissed an action seeking to enjoin the collection of taxes alleged to violate state and federal law. The Missouri court held that the plaintiff instead should have sought relief with a state tax commission, notwithstanding a previous ruling by the Missouri court that the commission had no power to consider plaintiff's complaint. The plaintiff (like petitioner in this case) promptly filed a petition for rehearing, arguing that the decision effectively deprived it of any opportunity to present its claims for a fair resolution. When the Missouri court (like the court below), dismissed the petition for rehearing without opinion, this Court granted a petition for certiorari and reversed, explaining: "[T]he judgment of the Supreme Court of Missouri * * * has denied to the plaintiff 'due process of law' – using that term in its primary sense of an opportunity to be heard and to defend its substantive right." 281 U.S. at 678. Addressing the concern that the primary basis for plaintiff's original complaint had been a question of state law, this Court explained:

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case."); Note, *Appellate Sua-Sponte Activity: Remaking Disputes and the Rule of Non-Intervention*, 40 S. CAL. L. REV. 352, 363 (1967) ("Due process is denied by an appellate court which decides on grounds it has raised sua sponte without giving the parties opportunity to be heard on those grounds."); *see also* ROBERT J. MARTINEAU, MODERN APPELLATE PRACTICE 41 (1983) ("Failure to hear the parties on the issue that determines their case comes close to a denial of basic due process."); Catherine T. Struve, *Direct and Collateral Federal Review of the Adequacy of State Procedural Rules*, 103 COLUM. L. REV. 243, 258 (2003) ("As *Brinkerhoff-Faris* suggests, novel state court rulings can implicate due process concerns if the result is that a litigant never gets an opportunity to be heard in response to the unanticipated ruling.").

> It is true that the courts of a state have the supreme power to interpret and declare the written and unwritten laws of the state; that this court's power to review decisions of state courts is limited to their decisions on federal questions; and that the mere fact that a state court has rendered an erroneous decision on a question of state law * * * does not give rise to a claim under the Fourteenth Amendment or otherwise confer appellate jurisdiction on this court.
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> * * * * Our present concern is solely with the question whether the plaintiff has been accorded due process in the primary sense – whether it has had an opportunity to present its case and be heard in its support.

281 U.S. at 680-81.[14] Because the Missouri Court had not provided that opportunity, this Court granted relief.

"The rule of law * * * is a[n] * * * entitlement of persons to have their behavior governed by rules publicly fixed in advance." *Landgrave v. USI Film Prods.*, 511 U.S. 244, 265 n.18 (1994) (*quoting* Stephen R. Munster, *A Theory of Retroactive Legislation*, 61 TEX. L. REV. 425, 471 (1982)). The proceedings in this case as it now stands do not satisfy that standard. Thus, we respectfully submit, "to hold that this sort of procedure constituted a meaningful 'chance to be heard in a trial of the issues,' *Cole v. Arkansas,* 333 U.S. 196, 201 (1948), is to make a mockery of the due process of law that is guaranteed every citizen," *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626,

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[14] *See also Ward v. Bd. of County Comm'rs*, 253 U.S. 17, 22-23 (1920) (holding that a "plainly untenable" nonfederal ruling is not an adequate justification for a deprivation of a federal right).

673 (1985) (Brennan, J., concurring in part and dissenting in part).

It is understandable that the Pennsylvania Supreme Court would wish to be sure that the important legal questions briefed and argued to the court were in fact presented by the record before proceeding to decide those questions. But customary appellate procedures offer a number of appropriate courses of action. The court could have dismissed the petition for allocatur as improvidently granted. The court could have remanded the case to the trial court for clarification of the record. The court could have sought additional briefing from the parties. At a minimum, the court could have given petitioner an opportunity to address these questions in open court.[15] We have no doubt that the court could not have issued the opinion that it did had the court questioned petitioner's counsel about these issues at the oral argument.

Any of those courses of action would have been plausible choices, which would not have implicated the Constitution in any cognizable way. The response of the court below, however, was the "'bait and switch' gambit"[16] condemned in *Brinkerhoff-Faris*. At bottom, the decision below reflects the force of the "gorilla rule" discussed by commentators – a rule that is acceptable because the Pennsylvania Supreme Court has the authority of a 500-pound gorilla in

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[15] *See* Miller, *supra*, 39 SAN DIEGO L. REV. at 1297-1301 (discussing responsible approaches to the problem); Milani & Smith, *supra*, 69 TENN. L. REV. at 294-314 (same).

[16] *See* Richard H. Seamon, *The Sovereign Immunity of States in Their Own Courts*, 37 BRANDEIS L.J. 319, 399 n.394 (1998) (characterizing *Brinkerhoff-Faris* as a decision holding that "the 'bait and switch' gambit * * * violated the Due Process Clause).

the way it treats litigants that appear before it. *See* Miller, *supra*, 39 SAN DIEGO L. REV. at 1279, 1310 ("The gorilla rule may be fine in the jungle. But it does little to create respect for law in the courthouse. It is time to use process to tame the gorilla.").[17] This Court stands as our last bulwark against such a transparent abandonment of the rule of law.

3. Although it is not directly relevant to the constitutional questions on which we seek review, it is important that the Court understand the notoriety that attended the proceedings in the courts below, so that the Court can understand the pressure that confronted the lower court to resolve the dispute in a manner that avoided controversy. The case was unusual in presenting both a large punitive damages award and a legal question of great commercial significance – neither of which was treated in the decision of the Pennsylvania Supreme Court. First, although the amount of the verdict had been overturned before the case reached that court, we believe that the verdict at trial was the largest verdict ever entered against a national bank in this country. On the merits, the specific substantive questions that remained drew the attention of numerous amici, including not only the Pennsylvania Chamber of Commerce and the Pennsylvania and American Bankers' Associations, but also all of the Federal Reserve Banks and Sysco Corporation. Similarly, numerous commentators had discussed and criticized the decision of the intermediate appellate court. Conversely, the *sua sponte* decision that had the apparently unintended side effect of invalidating industry reliance on bailee letters has led to widespread

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[17] The term apparently has its origin in Robert J. Martineau, *Considering New Issues on Appeal: The General Rule and the Gorilla Rule*, 40 VAND. L. REV. 1023 (1987).

consternation in the industry, including filings of amicus briefs in support of our application for reargument by major warehouse lenders concerned about the substantive effects of the decision.[18] The gravity of the questions before the court below of course cannot justify the failure of process discussed above, but we do think it can help this Court to understand what has occurred in the proceedings below.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

RONALD J. MANN
MAURICE R. MITTS

March 2005

[18] *E.g.*, Stephen C. Veltri, et al., *Payments*, 58 BUS. LAW. 1575, 1598-1603 (2003); HENRY J. BAILEY, III & RICHARD B. HAGEDORN, BRADY ON BANK CHECKS: THE LAW OF BANK CHECKS ¶ 15.16[1]; BARKLEY CLARK & BARBARA CLARK, THE LAW OF BANK DEPOSITS, COLLECTIONS AND CREDIT CARDS ¶ 17.06[2] (Dec. 2004 update); BARKLEY CLARK & BARBARA CLARK, THE LAW OF SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE ¶ 3.11[3] (Dec. 2004 update); Barkley Clark & Barbara Clark, *Bank Has Broad Right to Exercise Setoff Against Funds Wired into Beneficiary's Account*, 09-04 CLARK'S BANK DEPOSIT & PAYMENTS MONTHLY (Sept. 2004).

[J-62-2004]
IN THE SUPREME COURT OF PENNSYLVANIA
EASTERN DISTRICT

PIONEER COMMERCIAL FUNDING CORP. AND BANK ONE, TEXAS, N.A.	:	No. 53 EAP 2003
v.	:	Appeal from the Order entered on 3/18/02 in Superior Court at No. 144 EDA 2001 affirming in part, reversing in part and remanding (Reargument denied on 5/21/02) the Judgment entered on 12/21/00 in the Court of Common Pleas, Civil Division of Philadelphia County at No. 885 April term 1998
AMERICAN FINANCIAL MORTGAGE CORP. AND THOMAS F. FLATLEY AND NORTHWEST FUNDING, INC. AND CORESTATES BANK, N.A.	:	
APPEAL OF: CORESTATES BANK, N.A.	:	ARGUED: April 13, 2004

OPINION

MR. JUSTICE SAYLOR **DECIDED: August 19, 2004**

This appeal is centered on a commercial priority dispute between a banking institution exercising setoff against a general deposit account and a company asserting a third-party interest in the account proceeds, in the nature of absolute ownership and/or a perfected security interest.

Appellee, Pioneer Commercial Funding Corp. ("Pioneer") is a publicly-traded company that operated as a real estate warehouse lender in California. As such, Pioneer

provided funding to small-to medium-sized companies originating loans to home buyers.[1] Pioneer obtained its own primary funding via a line of credit extended by a consortium of lenders operating through a Texas financial institution known as Bank One Texas, N.A. ("Bank One").

In the usual course of affairs, loan originators receiving funding from Pioneer repaid their obligations using the proceeds from bulk sales of the loans to one or more third-party investors comprising a secondary market, thus enabling Pioneer to meet its own obligations to Bank One. Pending such sales, under the terms of loan and security agreements, Pioneer maintained a security interest in, *inter alia*, the original promissory notes signed by home buyers, as well as proceeds from their sale.[2] Perfection was accomplished by means of possession of the negotiable instruments in bearer form – as home purchase transactions closed, the loan originators endorsed the notes in blank and delivered them to Pioneer, together with blank assignments and other security documentation.[3] Pursuant to a three-party agreement between Pioneer, the loan originator, and Bank One, Pioneer delivered these collateral packages to Bank One, to secure Pioneer's own credit

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[1] *See generally Regions Bank v. Provident Bank, Inc.*, 345 F.3d 1267, 1270-71 (11th Cir. 2003) (setting forth a succinct description of the warehouse lending practices); 2 BARKLEY CLARK, THE LAW OF SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE ¶7.08[2][b] (1999) (same).

[2] *See* 13 Pa.C.S. §1201 (defining "security interest" as "an interest in personal property or fixtures which secures payment or performance of an obligation"); 13 Pa.C.S. §9203(f) (providing for attachment of a security interest in proceeds from the sale of collateral).

[3] *See* 13 Pa.C.S. §9313 (providing for perfection by possession). *See generally* 2 CLARK, THE LAW OF SECURED TRANSACTIONS ¶7.08[2][b].

line pending the resale.[4] Upon the resale, the notes were endorsed and transmitted to the purchaser with a shipping request (including wiring instructions for the sale proceeds) and bailee letter, a document employed as a general convention in the warehousing lending industry to permit a secured creditor to release possession of negotiable instruments to prospective purchasers without surrendering perfection.[5] The purchaser, in turn, wired funds to a restricted Pioneer account at Bank One, and Bank One was repaid from that account, thus completing the transaction.

At the center of this litigation is a business arrangement that was markedly different from Pioneer's usual course dealings, involving a California loan originator known as RNG Mortgage Services, Inc. ("RNG") and American Financial Mortgage Corporation ("AFMC"), a Pennsylvania company in the same business. As background, in the spring of 1997, Pioneer committed to serving as RNG's warehouse lender, and the companies executed loan and security and three-party agreements

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[4] Under the three-party agreement, Bank One held the collateral as agent for its consortium of lenders, Pioneer, and the loan originator.

[5] *See* 13 Pa.C.S. §9313(h); *see also* 13 Pa.C.S. §9-305 (superseded). *See generally* WILLIAM B. HAWKLAND, 9B HAWKLAND UNIFORM COMMERCIAL CODE SERIES §9-313:4 (2002); 2 CLARK, THE LAW OF SECURED TRANSACTIONS §7.08[2][b] (describing the bailee-with-notice concept underpinning Section 9-313(h) as a "dependable and commercially reasonable method to maintain perfected status on third-party notes that are in the possession of prospective investors" and a "critical legal device for the warehouse lending industry."). A true bailment is a specific-purpose transfer of possession only, in which absolute ownership remains in the bailor. *See generally Smalich v. Westfall*, 440 Pa. 409, 413, 269 A.2d 476, 480 (1970); 8A AM JUR. 2D BAILMENTS §15 (2003).

establishing the usual governing terms and conditions. This relationship, however, was compromised after August of 1997, when RNG sought protection under Chapter 11 of the federal Bankruptcy Code. RNG's financial condition impaired its ability to attract investors from the secondary market, given its inability to assure them recourse, thus threatening its ability to survive as a going concern. About the same time as RNG was seeking avenues to allow it to continue its operations, AFMC was exploring expansion opportunities. Learning of RNG's circumstances, AFMC began investigating a possible acquisition of the California company's assets, the most valuable of which was its portfolio of unfunded mortgage commitments, referred to in the industry as a loan "pipeline."

Both AFMC and RNG thus had an interest in maintaining RNG as a going concern while AFMC considered the acquisition. To accomplish this, they devised an arrangement whereby AFMC would receive an effective assignment of the loans, assume recourse responsibility relative to them, and sell them in the secondary market. Pioneer was also made a party to the discussions, as AFMC and RNG desired to obtain continued funding from Pioneer for loans in the pipeline. Pioneer elected to participate for its own reasons, apparently related to its desire to obtain the existing business and the prospect of a future warehouse lending relationship with AFMC.

The dispositive issue in this appeal concerns the nature of the interest conferred upon AFMC in this arrangement, and, relatedly, the character of the interest reserved to Pioneer. Mechanically, Pioneer and AFMC executed a loan and security agreement and a three-party agreement (with Bank One), thus facially establishing the framework of a debtor/creditor relationship. Pioneer

agreed to arrange for the notes to be endorsed and shipped to AFMC, along with a bailee letter indicating that Pioneer held a security interest in the notes and their proceeds, and also, retained title pending full payment.[6] AFMC, in turn, was to consummate the sale to an institutional investor, and Pioneer was to be paid from the proceeds. Additionally, RNG committed to obtaining approval of this arrangement from the federal bankruptcy court supervising its operations.[7]

RNG assembled the first loan portfolio to be administered in this manner, worth approximately $2.3 million, in mid-October of 1997. AFMC proceeded to obtain a purchase commitment from Norwest Funding, Inc. ("Norwest"), an institutional investor that had categorically refused to purchase loans directly from RNG. In connection with the purchase, Norwest required a series of seller representations and warranties, including AFMC's attestation to its absolute and unencumbered ownership of the notes, which facially contradicted the bailee letter transmitted from Pioneer to AFMC. The notes were released to AFMC, endorsed by it, and shipped by AFMC to Norwest.[8] After reviewing the notes, Norwest subsequently transferred payment for those that it accepted via the Federal Reserve Wire Transfer Network ("FedWire") to an AFMC account maintained with Appellant, CoreStates

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[6] Pioneer also obtained personal guarantees from AFMC's principal, Thomas Flatley, as well as RNG's principal.

[7] Parenthetically, RNG failed to obtain this approval as promised.

[8] The parties maintain a factual dispute concerning whether or not AFMC also forwarded the bailee letter to Norwest. Resolution of this dispute is not material to our disposition of the appeal, infra.

Bank, N.A. ("CoreStates"),[9] which had been denominated by AFMC as a "settlement account." Upon AFMC's request, CoreStates forwarded the funds to Bank One, to the credit of Pioneer's designated account.

After the first transaction, Pioneer expressed concern about AFMC's possession of the proceeds from the loan sales and requested that AFMC instruct Norwest to transmit proceeds from future sales directly to Pioneer's account at Bank One. Representatives of Pioneer, RNG, and AFMC all contacted Norwest to convey Pioneer's request.

As it turns out, Pioneer's concern was well founded, since, unbeknownst to it or AFMC, CoreStates was beginning an investigation of account activity of corporations in which AFMC's principal, Thomas Flatley, had an interest. The bank had discovered a substantial overdraft in an AFMC account, in the amount of approximately $4.5 million, and, as a result of its investigation, concluded the overdraft was a consequence of a sustained practice of check kiting, *i.e.,* improper manipulation of accounts to allow the account holder to draw on funds that it did not in fact possess.[10] In response, on November 7, 1997, CoreStates imposed debit restraints on Flatley company accounts, including the AFMC settlement account.

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[9] In April of 1998, CoreStates merged with First Union National Bank, which became the successor-in-interest to its position in this litigation. For convenience, we will refer to the Appellant as CoreStates throughout.

[10] Pursuant to a cash management agreement with CoreStates, funds accumulated in any of AFMC's accounts could be used to cover checks drawn on other accounts. However, the series of overdrafts resulting in AFMC's ongoing indebtedness of $4.5 million was well beyond the scope of such agreement.

Without knowledge of this debit restraint, RNG, Pioneer, AFMC, and Norwest proceeded with the sale of a second portfolio of loans to Norwest, this time valued at approximately $1.78 million, which occurred during the second week of November, 1997. The second transaction initially proceeded much as the first one had. Contrary to Pioneer's expressed wishes, and despite the request that AFMC had previously conveyed on Pioneer's behalf, AFMC again furnished instructions to Norwest to wire the proceeds of the sale to AFMC's self-described settlement account at CoreStates. Norwest complied with those instructions and transmitted the approximately $1.78 million to this account via FedWire in three installments. These funds became frozen as a result of CoreStates' debit restraint, and CoreStates refused requests from the various parties to either return the monies to Norwest or to forward them to Pioneer's account at Bank One.

Later that month, CoreStates consulted a specialist in banking law in connection with the AFMC overdrafts. The attorney advised the bank that it had the right to set off monies credited to AFMC deposit accounts against the overdraft indebtedness.[11] CoreStates subsequently swept and closed AFMC's accounts, including the settlement account, making corresponding entries in its books to afford AFMC credit against its indebtedness. In the ensuing months, CoreStates negotiated repayment terms with Mr. Flatley for the remainder of the indebtedness,

[11] A bank's right of setoff arises under common law, subject to requirements of mutuality of obligation, maturity, deposit in a general account, and depositor ownership. *See Royal Bank of Pa. v. Selig,* 434 Pa. Super. 537, 546, 644 A.2d 741, 744 (1994). It is undisputed that the first three of these four elements were met; the depositor ownership element, however, is a central subject of the remaining controversy.

which culminated in a workout agreement executed in March of 1998.

Pioneer, for its part, would no longer fund RNG, and RNG ceased doing business. Although Pioneer never received payment in relation to the second loan portfolio, it satisfied its own indebtedness to Bank One. Apparently as a result of a downward spiral triggered by its substantial losses in this regard, however, Pioneer itself ceased doing business in the summer of 1999.

Pioneer commenced the present civil action against CoreStates, AFMC, Flatley, and Norwest, in 1998. The primary claim against CoreStates was grounded in a theory of conversion,[12] and Pioneer also sought punitive

[12] An obstacle to the assertion of a claim of conversion against a bank exercising a right of setoff of the proceeds of a general deposit account arises out of the debtor/creditor relationship between the bank and the account holder. Among the essential elements of conversion is an absence of owner consent. *See Stevenson v. Economy Bank of Ambridge,* 413 Pa. 442, 451, 197 A.2d 721, 726 (1964) (setting forth the elements of a conversion claim). As a general rule, however, general deposit account proceeds are treated as property of the bank, with account balances representing the bank's indebtedness to the depositor. *See Thomas v. First Nat'l Bank of Scranton,* 376 Pa. 181, 184, 101 A.2d 910, 911 (1954). Thus, at least in the usual case, owner consent will be inherent in the act of bank setoff. *See generally* 14 CAUSES OF ACTION 105 §3 (2004); 1 THOMAS D. CRANDALL, RICHARD B. HAGENDORN, AND FRANK W. SMITH, THE LAW OF DEBTORS AND CREDITORS §5.12 (2004) ("The action against a bank for improper setoff should lie in breach of contract, as opposed to the tort of conversion."). Conversion theory, however, has been invoked in other jurisdictions as a means of vindicating third-party ownership interests in certain identifiable account proceeds. *See, e.g., Citizens Nat'l Bank v. Mid-States Dev. Co.,* 380 N.E.2d 1243, 1248-50 (Ind. App. 1978); *cf.* 14 CAUSES OF ACTION 105 §3 (2004) ("A conversion action is clearly proper where the plaintiff is alleging that the funds set off by the bank comprised a deposit for a special purpose."). *See generally* Dag Wilkinson, *Third-Party Interests in Deposit Accounts and the Bank's Right of Setoff,* 109 BANKING L.J.

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damages. In the pretrial proceedings, Corestates unsuccessfully sought dismissal of the action and, subsequently, summary judgment. Among other theories, CoreStates invoked decisional law holding that a bank's common law right of setoff has priority over a perfected security interest in collateral.[13] *See Pennsylvania Nat'l Bank & Trust Co. v. CCNB Bank N.A.*, 446 Pa. Super. 625, 630-32, 667 A.2d 1151, 1154-55 (1995), *limited appeal allowed,* 544 Pa. 195, 675 A.2d 1209 (1996).[14] Pioneer, on the other hand, relied substantially on a line of cases vindicating the interests of third-party owners over a bank's right of setoff, where the account holder possesses the third-party funds strictly as a fiduciary or agent. *See, e.g., Sherts v. Fulton Nat'l Bank,* 342 Pa. 337, 340-41, 21 A.2d 18, 20 (1941).[15]

No. 3 (May-June 1992) ("A bank improperly exercising setoff, in violation of a third-party interest in a deposit account, may open itself up to an action for conversion, including claims for attorney fees and possible punitive damages.").

In light of our disposition, below, we need not proceed further with an analysis of the appropriateness of conversion theory to Pioneer's averments in this case, which, in any event, is beyond the scope of the questions framed by CoreStates for our review in its statement of questions involved. *See* Pa.R.A.P. 2116(a).

[13] Under the Uniform Commercial Code, as reflected in the Pennsylvania Commercial Code, perfection of a security interest is maintained in identifiable proceeds upon the sale of collateral. *See* 13 Pa.C.S. §9315(a)(2). Whether proceeds are capable of identification is determined according to common law tracing rules. *See id.* cmt. 3. Here, the proceeds from the sale of the second loan portfolio to Norwest remained clearly identifiable, by virtue of CoreStates' debit restraint.

[14] The discretionary appeal allowed by this Court in *Pennsylvania National Bank & Trust* was subsequently discontinued without opinion.

[15] *Accord* 9 C.J.S. BANKS AND BANKING §309 (2004) ("Where the money deposited does not belong to the depositor, a set-off by the bank is improper, at least where the bank has notice of the third party's interest."). Application of the *Sherts* precept does not necessarily

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The trial court, however, took the view that such distinctions, and other principles of commercial law arising under the Pennsylvania Commercial and Banking Codes, were of little or no relevance to this case, primarily on the basis that Pioneer had grounded its action in the tort of conversion as opposed to commercial law. *See, e.g.*, N.T., June June [sic] 30, 2000 (a.m.), at 6 ("The action . . . is not in contract. It's absolute tort. Therefore, the UCC . . . do[es] not apply to this case. That applies only to contract actions."). Accordingly, as the case proceeded through trial,[16] the trial court refused CoreStates' request for a directed verdict grounded in these principles and its proposed jury instructions embodying them. Instead, the trial court issued a relatively short set of instructions that did not differentiate between (and indeed conflated)

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require that the third-party funds be reposited in a special or restricted account. *See, e.g., Ryan Bros., Inc. v. Curwensville State Bank*, 382 Pa. 248, 254-55, 114 A.2d 178, 181 (1955). Moreover, the parties devote substantial argumentation to the question of the timing of CoreStates' setoff, given that CoreStates' knowledge concerning the source of the AFMC funds increased over time in the period between its initial receipt of the sale proceeds from Norwest and the sweeping of the accounts (this discussion is centered on the application of the doctrine of automatic setoff, *see generally Selig*, 434 Pa. Super. at 545, 644 A.2d at 744). It is clear, however, that from the outset, CoreStates was aware that AFMC had denominated the relevant account a "settlement account"; this in and of itself is sufficient to trigger at least further inquiry under the *Sherts* line. *See Ryan Bros.*, 382 Pa. at 254-55, 114 A.2d at 181 (characterizing a plaintiff's case for resisting bank setoff under *Sherts* as particularly strong, where actual ownership was invested in the third-party plaintiff, and the account had been labeled a "distribution account"). Therefore, the focus of our analysis in this case is on the ownership, rather than the timing, aspect.

[16] Trial proceeded with Pioneer as the sole plaintiff (Bank One discontinued its claims prior to trial), against CoreStates, AFMC, and Flatley, with Pioneer settling its claims against Norwest immediately prior to trial.

possession by a fiduciary or agent subject to another's absolute reservation of title (a true trust or bailment arrangement and the *Sherts* paradigm) and a perfected security interest in account proceeds (the *Pennsylvania National Bank & Trust* scenario). The court then described Pioneer's essential claim as an assertion of a security interest in the AFMC account proceeds, and relegated CoreStates' defenses to the claim that Pioneer simply had no security interest.[17] Having reduced the issue to be decided by the jury to the single question of whether or not Pioneer possessed a security interest, the trial court advised the jurors that, if they answered this question in the affirmative, CoreStates had no right to set off and could be found liable for conversion.[18] Additionally, the court issued a generalized punitive damages charge.

In the context of the court's charge, the jury returned a special verdict finding that Pioneer possessed an ownership interest in the funds deposited in the AFMC settlement account. The jurors thus found Corestates and AFMC liable in conversion, and awarded Pioneer the $1.78

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[17] Although this certainly was one of CoreStates' defenses (arising from RNG's failure to obtain bankruptcy court approval of the Pioneer/AFMC/RNG transaction, *see supra* note 7), as previously indicated, CoreStates had plainly advanced, *inter alia,* the alternative position that even if Pioneer's interest in the account funds constituted a perfected security interest, prevailing Pennsylvania law afforded priority to its right of setoff. *See Pennsylvania Nat'l Bank & Trust,* 446 Pa. Super. at 630-32, 667 A.2d at 1154-55.

[18] The trial court also charged that CoreStates could be liable for conversion if the AFMC settlement account constituted a special or restricted, as opposed to a general, account. *See generally Royal Bank of Pa. v. Selig,* 434 Pa. Super. 537, 546, 644 A.2d 741, 745 (1994). The jury, however, returned a finding that the account was general in character, and this finding is not at issue in the present appeal.

million sum that CoreStates had set off.[19] The jury also found Corestates (but not AFMC) liable for punitive damages, and, after a damages phase of trial, awarded Pioneer an additional $13.5 million in consequential damages (the amount by which its market capitalization had declined between the date of setoff and the date of trial), and set the punitive damages award at $337.5 million.

In response to post-trial motions by Corestates, the trial court sustained the liability findings and the compensatory damages award, but remitted the punitive damages to $40.5 million, resulting in a judgment in favor of Pioneer in the amount of approximately $56 million. In an opinion accompanying its order, the court reiterated its view that the Pennsylvania Commercial and Banking Codes were inapplicable, since Pioneer's claim arose in tort. *See Pioneer Commercial Funding Corp. v. American Fin. Mortgage Corp.*, 50 Pa. D.&C.4th 31, 46 (C.P. Phila. 2000). Further, as in its instructions to the jury, the court also continued to conflate the concept of a security interest with absolute ownership, at various points describing the jury's finding as confirming Pioneer's absolute title to the funds, *see, e.g., id.* at 35 ("In the view of Pioneer, supported by this jury's verdict, Pioneer enjoyed the exclusive right of ownership in the sums . . . wired into AFMC's account."), and at others indicating that the jury's finding of ownership was based on the presence of a perfected security interest. *See, e.g., id.* at 42-43 ("The plaintiffs correctly characterize this ownership interest as a 'perfected security interest' vesting rights independently in Pioneer.").

[19] The trial court also had directed a verdict against AFMC and Flatley for this sum based on a contract theory.

The court at no time cited or discussed the relevance of *Pennsylvania National Bank & Trust* (which was again highlighted by CoreStates in the post-trial briefing), in light of its acknowledgement that the jury's determination of ownership was based entirely on a finding of a secured status.

Pioneer did not appeal the remittitur, but Corestates lodged an appeal in the Superior Court, where a divided panel affirmed as to liability, but awarded a retrial on the issue of punitive damages. *See Pioneer Commercial Funding Corp. v. American Fin. Mortgage Corp.*, 797 A.2d 269 (Pa. Super. 2002). With regard to CoreStates' position that the trial court conflated the absolute-title-retention versus sale-on-credit paradigms, the majority stated as follows:

> The jury . . . did not confuse any interests which AFMC may have had in the Fund with Pioneer's interest. The jury's understanding was clearly shown in its affirmative answer to the following question: "Do you find that plaintiff Pioneer Commercial Funding Corporation had an ownership interest in the funds wired by Norwest to American Financial Mortgage Corporation's settlement account at defendant CoreStates Bank that entitled plaintiff to possession of the funds?"

Id. at 284. The majority did not squarely address CoreStates' contention that the trial court's instructions did not appropriately frame the ownership question; in this respect, it merely characterized CoreStates' argument as

nothing more than an invitation to read isolated portions of the jury charge out of their appropriate context. *See id.*[20]

We allowed CoreStates' subsequent appeal, in which it has maintained, *inter alia,* that the jury's verdict was tainted by the common pleas court's decision to depart from prevailing principles of commercial law on the basis that such precepts lack relevance to a tort action grounded in conversion theory.

It is apparent from the outset that CoreStates' position in this regard has merit. As noted, the present matter at its core embodies a commercial priority dispute. Pioneer's styling of the action under the rubric of conversion did not undermine the relevance of governing principles of commercial law, since a claim of conversion cannot be sustained in the face of lawful justification on the part of the asserted tortfeasor. *See Stevenson v. Economy Bank of Ambridge,* 413 Pa. 442, 451, 197 A.2d 721, 726 (1964) ("A conversion is the deprivation of another's right of property in, or use or possession of, a chattel, or other interference therewith, without the owner's consent *and without lawful justification.*" (citation omitted)).[21] The trial court's ruling that tenets of commercial law were irrelevant improperly relieved Pioneer of establishing an essential element of its

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[20] Judge Beck dissented, concluding that Pioneer's conversion claim was preempted by the fund transfer provisions of the Pennsylvania Commercial Code, 13 Pa.C.S. §§4A101-4A507, discussed infra.

[21] Identifiable funds are deemed a chattel for purposes of conversion. *See, e.g., McKeeman v. Corestates Bank, N.A.,* 751 A.2d 655, 659 n. 3 (Pa. Super. 2000); *Francis J. Bernhardt, III, P.C. v. Needleman,* 705 A.2d 875, 879 (Pa. Super. 1998).

case (the absence of lawful justification), and wrongfully stripped CoreStates of relevant defenses.[22]

Furthermore, the case was submitted to a jury lacking essential direction. Because of the trial court's approach, the jury never learned of the relevant distinction under Pennsylvania law between the *Sherts* scenario, involving pure fiduciary or agency relationships entailing absolute retention of title, and a sale-on-credit transaction. Indeed, the trial court misled the jury by affirmatively indicating, contrary to the holding of *Pennsylvania National Bank & Trust,* that a security interest created a sufficient ownership interest to defeat a bank's right of setoff.[23]

The Superior Court majority's view (that the jury's finding of ownership in Pioneer demonstrated that it

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[22] The trial court was correct only to the extent that its ruling reflected the principle that, under prevailing Pennsylvania law, the Uniform Commercial Code did not supply the relevant priority rule. *See Pennsylvania Nat'l Bank & Trust,* 446 Pa. Super. at 631, 667 A.2d at 1154. It was not justified, however, in utilizing this principle to discount the relevance of the Uniform Commercial Code generally (for example, in the initial assessment of the character of Pioneer's interest at issue), or to diminish the relevance of other principles of commercial law as they pertained to the lawfulness of CoreStates' conduct.

[23] The trial court also was not wholly incorrect in its understanding that a security interest, in the broadest sense, carries with it ownership attributes. *See, e.g.,* Thomas W. Merrill & Henry E. Smith, *The Property/Contract Interface,* 101 COLUM. L. REV. 773, 834-35 (2001) (describing the property and contractual aspects of a security interest). The trial court's mistake was in not apprehending that it is not the type of interest that had been deemed, under Pennsylvania law, to be sufficient to defeat a bank's right of setoff. On this point, the trial court was not free to attempt to write on a clean slate. *See, e.g., In re Townsend's Estate,* 349 Pa. 162, 168, 36 A.2d 438, 441 (1944) (stating the precept that common pleas courts are bound by decisions of the intermediate appellate courts, in absence of a pronouncement by this Court on the subject matter of the decision).

understood the distinction between absolute ownership and security interests) is unsupportable, since the jury repeatedly was told by the trial court that a security interest constituted a sufficient ownership interest to support liability. Furthermore, its suggestion that such admonitions were isolated ones is not defensible – they were in fact the sum and substance of the trial court's description of the governing law in its liability instruction.

In its brief, Pioneer contends that *Pennsylvania National Bank & Trust* is not persuasive, and therefore, this Court should take this opportunity to overrule it. First, Pioneer argues that its analysis of the priority question is *dictum,* because the bank asserting its right of setoff "apparently" had previously relied on the deposit as security in making a loan to the debtor. This asserted fact, however, is neither apparent on the face of the *Pennsylvania National Bank & Trust* opinion nor is it any part of the Superior Court's express reasoning; therefore, we do not deem it a proper basis to displace the court's holding. Second, Pioneer takes the position that the case should be limited to its facts, as it involved bank setoff in relation to a certificate of deposit as opposed to a deposit account. The certificate of deposit at issue, however, was of the non-negotiable variety, which has been held to constitute a general deposit account under the prior version of the Uniform Commercial Code, *see, e.g., In re Alabama Land and Mineral Corp.,* 292 F.3d 1319, 1324-25 (11th Cir. 2002), and notably, this treatment has been made express under the revised Uniform Commercial Code. *See* 13 Pa.C.S. §9102, cmt. 12 (stating that "[t]he revised definition [of deposit account] clarifies the proper treatment of nonnegotiable or uncertificated certificates of deposit," and observing that, unless of a type subject to transfer by

delivery only without endorsement or assignment, a non-negotiable certificate of deposit is a deposit account).[24] Moreover, the *Pennsylvania National Bank & Trust* court obviously viewed non-negotiable certificates of deposit and deposit accounts as being of the same order, since it predicated its decision on a series of decisions involving bank setoff of deposit accounts. *See Pennsylvania Nat'l Bank & Trust,* 446 Pa. Super. at 629-31, 667 A.2d at 1154 (citing, *inter alia, Pittsburgh Nat'l Bank v. United States,* 657 F.2d 36, 38 (3d Cir. 1981); *Selig,* 434 Pa. Super. at 537, 644 A.2d at 744; *Aarons v. Pub. Serv. Bldg. & Loan Ass'n,* 318 Pa. 113, 178 A. 141 (1935)).

We appreciate the complexity of the priority issue resolved in *Pennsylvania National Bank & Trust,* and acknowledge the strong equities attaching to each of the competing interests as between banking institutions and companies funding purchase transactions in general commerce. We are also aware that the *Pennsylvania*

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[24] Pioneer also invokes a prior Superior Court decision, *Middle Atlantic Credit Corp. v. First Pa. Banking and Trust Co.,* 199 Pa. Super. 456, 185 A.2d 818 (1962), as establishing the appropriate priority of a perfected-secured creditor over a bank exercising a right of setoff. Although certainly there is language in *Middle Atlantic* supporting Pioneer's position, the case concerned a factoring relationship in which the funds in issue had been assigned to the plaintiff, and the holding was expressly grounded in the *Sherts* decision pertaining to funds held in trust. *See Middle Atlantic,* 199 Pa. Super. at 457-58, 185 A.2d at 819. Additionally, as Pioneer's argument acknowledges, *Pennsylvania National Bank & Trust* represents the more recent decision on the priority accorded to bank setoff. Notably, since rendering the decision, the Superior Court has continued to frame its holding in broad terms. *See, e.g., Commercial Nat'l Bank, of Pa. v. Seubert & Assoc., Inc.,* 807 A.2d 297, 308 (Pa. Super. 2002) ("In *Pennsylvania Nat'l Bank and Trust Co.,* we affirmed the trial court's grant of summary judgment and held that the common-law setoff right gave the bank a right to self-help that took priority over other creditors claiming a right to the funds.").

National Bank & Trust panel afforded little in the way of concrete explanation concerning the balance that it struck in devising a common law priority rule.[25] To some degree, the inability to fully rationalize a particular priority structure is inherent in the nature of the undertaking – it is perhaps best conceptualized as an attempt to establish a framework pursuant to which parties can organize their financial dealings on a prospective basis with a fair degree of predictability. As such, and given the range and scale of interests involved, the exercise is far more amenable to legislative determination than to common law decision making. Indeed, as Pioneer acknowledges, legislative intervention did in fact occur – in 1998, the Uniform Commercial Code was revised to embrace the *Pennsylvania*

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[25] Prior to 1998 amendments to the Uniform Commercial Code, there was in fact a fairly strong current in a number of other jurisdictions favoring the interests of secured creditors over depository institutions, based on the general priority provision of Article 9. *See* Pa.C.S. §9201(a) ("Except as otherwise provided by this Act, a security interest is effective according to its terms between the parties, against purchasers of the collateral and against creditors."). *See generally* Annotation, *Effect of UCC Article 9 Upon Conflict, As to Funds in Debtor's Bank Account, Between Secured Creditor and Bank Claiming Right of Setoff*, 3 A.L.R. 4th 998 (2004) (collecting cases); Janet A. Flaccus, *Banks Against Secured Parties To The Victors Go The Spoils*, 6 U. MIAMI BUS. L. J. 59, 59 (1997) (observing that "the priority battle between banks claiming an interest not created under Article Nine and secured parties has split the courts"). The contrary line of cases generally relied on the exclusion of prior UCC Section 9-104(i) (excluding from the coverage of Article 9 a transfer of any "deposit, savings, passbook, or like account with a bank, savings and loan association, credit union, or like organization"), to exempt setoff from consideration under Article 9 entirely and to interpose a common law priority rule. *See id.; see also* Annotation, *Effect of UCC Article 9 Upon Conflict, As To Funds In Debtor's Bank Account, Between Secured Creditor And Bank Claiming Right Of Setoff*, 3 A.L.R. 4th 998 §1 (1981); Flaccus, *Banks Against Secured Parties*, 6 U. MIAMI BUS. L.J. at 64.

National Bank & Trust holding, *see* 13 Pa.C.S. §9-340(a) (establishing the general rule that "a bank with which a deposit account is maintained may exercise any right of recoupment or set-off against a secured party that holds a security interest in the deposit account"), which has since been adopted in fifty states.[26]

Thus, the Pioneer/AFMC arrangement for sale of the second loan portfolio to Norwest was orchestrated at a time when Pennsylvania's common law matched the Uniform Commercial Code's present, statutory priority scheme, and, as reflected in that scheme, and taking due consideration of the respective interests involved, the common law priority scheme was at least a reasonable one. In these circumstances, we do not believe that the interests of justice require further evaluation of the potential for retrospectively modifying the now-supplanted common law to consider the wisdom of a closed-ended departure from current practice.

In summary, under prevailing Pennsylvania law as it existed at the time of trial, the controlling question in this case should have been whether Pioneer effectuated an absolute reservation of title in the second loan portfolio and its proceeds (i.e., a true bailment), versus whether it possessed a perfected security interest (or something of

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[26] *See generally* 1 CLARK, THE LAW OF SECURED TRANSACTIONS ¶1.08[9][c] ("Rev. UCC §9-340 . . . changes prior law in most states by giving priority to a bank's right of setoff over a security interest in a deposit account claimed by another creditor."); 11 LARRY LAWRENCE, ANDERSON ON THE UNIFORM COMMERCIAL CODE §9-340:4R (2003) (observing that, under the revised UCC, "the bank may set off a debt owed to it by the debtor even though another secured party also has a security interest in the account"). The statutory amendment was effectuated in Pennsylvania in 2001.

lesser priority). Since the common pleas court failed to make this distinction, at a minimum, the verdict must be vacated and the case returned for a new trial.

CoreStates also seeks review of the trial court's decision to deny it judgment notwithstanding the verdict on the ground that, as a matter of law, Pioneer's interest should be relegated, at most, to the security-interest category. In this undertaking, we review the record in the light most favorable to Pioneer to assess whether its evidence was sufficient to sustain the bailment theory. *See Adamski v. Miller,* 545 Pa. 316, 319, 681 A.2d 171, 173 (1996).

As a threshold matter, we recognize that Article 9 of the Uniform Commercial Code was conceived with the goal of minimizing the role of actual, technical title in the governance of commercial transactions. *See generally* 13 Pa.C.S. §9202 (stating the general rule that the provisions of Article 9 "apply whether title to collateral is in the secured party or the debtor"); Charles W. Mooney, Jr., *The Mystery and Myth of 'Ostensible Ownership' and Article 9 Filing,* 39 ALA. L. REV. 683, 789 n. 275 (1988) ("one of the basic conceptual underpinnings of Article 9 [is] the unification of treatment of all secured transactions that have the same economic effect without making unnecessary distinctions based on the form of the transaction or the location of 'title.'"); 9B HAWKLAND UNIFORM COMMERCIAL CODE SERIES §9-202:1. Significantly, parties are not constrained, however, in all instances to conduct their affairs under the Uniform Commercial Code's regime; for example, a true bailment relationship (a directed-purpose transfer to an agent of possession only, subject to absolute retention of title), is not covered by Article 9. *Accord* 8 HAWKLAND UNIFORM COMMERCIAL CODE SERIES §9-102:3 (citing

Rohweder v. Aberdeen Prod. Credit Ass'n, 765 F.2d 109, 112 (8th Cir. 1985)). In distinguishing between transactions governed by the Uniform Commercial Code versus those controlled by other law (here, a sale on credit versus a true bailment), the intention of the parties is obviously the preeminent consideration. To assess intent, courts will look not to any particular document or the form of the transaction, but rather, to the overall transaction and its substance. *See generally* 13 Pa.C.S. §9-102, cmt. 3b.[27]

In the present case, Pioneer, RNG, and AFMC participated in an unusual transaction designed to invest in AFMC the accouterments of ownership vis-a-vis the second loan portfolio. The undisputed objective was to satisfy Norwest's condition that it have a right of recourse against the seller. Although the transaction was unique, it was nevertheless organized around a loan and security agreement, the cornerstone of a UCC-based security relationship, *see* 13 Pa.C.S. §9201, the notes were endorsed to AFMC, AFMC in turn endorsed the notes as the sole party entitled to their enforcement, and the transaction was held out to third parties as a sale with the knowledge of all concerned. The situation is in no way akin to that which was present in *Sherts,* namely, setoff of an attorney's deposit account containing proceeds from

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[27] *Cf.* 1 CLARK, THE LAW OF SECURED TRANSACTIONS ¶1.03[1] ("Since the key to coverage under Article 9 is *intent* to create a security interest, and since substance rules over form, the courts will look through a transfer absolute in form to find a secured transaction if that was the real intent of the parties."). These sorts of questions frequently arise in the Article 2 context in terms of sale versus leasing arrangements. *See, e.g.,* 1 THOMAS D. CRANDALL, RICHARD B. HAGENDORN, AND FRANK W. SMITH, JR., THE LAW OF DEBTORS AND CREDITORS §7:22 (2004); 8 HAWKLAND UNIFORM COMMERCIAL CODE SERIES §9-102:3; BANKRUPTCY SERVICE LAWYERS EDITION §49:243 (2004).

receivables belonging to third-parties. *See Sherts,* 342 Pa. at 338-39, 21 A.2d at 19. The overall structure of the transaction, therefore, militates strongly in favor of treating the transaction as a sale on credit, subject to a security interest.[28]

The strongest evidence of an intention on the part of Pioneer to retain absolute title is reflected in the bailee letter.[29] As noted, the bailee letter is a standard, commercial device designed to assure continued perfection of a security interest, *see supra* note 5; *see also* 2 CLARK, THE LAW OF SECURED TRANSACTIONS ¶7.08[2][b] ("By use of the bailee letter, [the warehouse lender] retains its perfected security interest in the third-party notes by a form of constructive possession."); it is not designed to create a true or pure bailment relationship. Moreover, in the circumstances presented, the assertion in the bailee letter of an absolute retention of title is inconsistent with the overall structure of the transaction – indeed, if it were to have been enforced, the proviso would have wholly undermined the sale of the second loan portfolio on the designated terms. We therefore agree with CoreStates that

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[28] In rejecting the possibility of a sale scenario, the trial court placed substantial emphasis on the fact that Pioneer did not receive contemporaneous payment from AFMC. *See, e.g.,* N.T., June 7, 2000 (p.m.), at 42 ("An ownership interest vests only upon payment."). The trial court's view, however, overlooks the myriad possibilities for styling a sale-on-credit transaction. It is also worth referencing the value accruing to AFMC for entering into such a relationship, in terms of maintaining RNG's status as a going concern and, concomitantly, AFMC's ability to benefit from RNG's assets via an acquisition.

[29] Of course, as CoreStates emphasizes, Pioneer had never formally been inserted into the chain of title; however, it (and/or Bank One as its agent) did maintain the notes in bearer form at the time the bailee letter was transmitted to AFMC.

to permit a factfinder to regard the trust proviso of the bailee letter as dispositive would afford too little recognition to the other documents and the overall character of the transaction. We also view the similar characterizations of the transaction by Pioneer's lay witnesses at trial as insufficient to overcome the understanding arising from the undisputed structure and purpose of the transaction.[30]

Accordingly, based on the evidence viewed in the light most favorable to Pioneer, we hold as a matter of law, that the transfer of the second loan portfolio to AFMC was in the nature of a sale-on-credit transaction, subject to a security interest, as opposed to a true bailment. As such, the case need not be returned for fact finding on this subject.

In considering whether there is any other reason to return the matter for a jury determination, we observe that the case had many facets. For example, the parties maintain a vigorous dispute concerning whether Norwest's transfer of the proceeds from the sale of the second loan portfolio to the AFMC account occurred by design or mistake. Along another line, the trial court's opinion is replete with criticisms of CoreStates' conduct giving rise to the litigation. *See, e.g., Pioneer,* 50 Pa. D.&C. 4th at 34-35 (stating that "CoreStates, in a desperate attempt to recoup its negligently incurred losses, seized the funds pursuant

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[30] Pioneer did offer testimony from an attorney, but it was presented as fact evidence – Pioneer offered no testimony from a qualified expert witness in the liability proceedings. Although CoreStates does not frame the matter on such terms, the absence of expert testimony to aid the jury in making the essential distinction between the various commercial relationships represents another substantial deficiency in Pioneer's position.

to its alleged right of setoff"); *id.* at 35 (indicating that "AFMC and Thomas Flatley entered into a workout agreement with the bank whereby the parties conspired to keep Pioneer's money and to keep the matter secret."). Although the case was not originally framed by the trial court for the jury determination to depend on such considerations, the question arises whether they may be relevant to the case as it could or should have been framed.

On the matter of CoreStates' conduct, it is significant that Pioneer did not undertake in the liability proceedings to establish any prevailing standards in the banking community that would support the characterization of the bank's conduct as negligent. This sort of perspective on the case, therefore, appears to arise more from a visceral reaction based on generalized notions concerning the relative equities of the parties' positions than from an application of governing legal principles. In this regard, although CoreStates' act of setting off the AFMC account was aggressive, particularly in light of the character of the underlying debt owed to it by its depositor, it simply did not exceed the limits of existing law. Similarly, the fact that CoreStates entered into a confidential agreement with Flatley to satisfy AFMC's remaining indebtedness after the setoff does not serve as a predicate for liability in conversion.

Regarding the aspect of whether or not the transfers to the AFMC settlement account occurred by mistake, there was some conflict in the evidence presented at trial, and therefore, fact finding would be implicated if the question were material to the outcome of the case. We conclude, however, that it is not. In terms of the lawful justification for its conduct, CoreStates was not bound by any particular party's characterization of the transfer as

mistaken. At most, the bank was on inquiry notice of a potential third-party interest (*inter alia* by virtue of AFMC's denomination of the relevant account as a "settlement account," *see supra* note 15), and was therefore bound to conduct a reasonable investigation. The undisputed evidence, however, is that CoreStates did, in fact, conduct that investigation, and, in the course of it learned of the transaction structured by Pioneer, RNG, and AFMC. Corestates thus discovered the facts underlying our conclusions that AFMC had been placed into the chain of title with respect to the second loan portfolio, and that Pioneer possessed at most a perfected security interest. Further, Corestates learned that AFMC had instructed Norwest to transfer the proceeds from the sale of the second loan portfolio to its settlement account. In view of these circumstances, the fact that Pioneer desired to be paid directly by Norwest, or even that Norwest may have at various junctures undertaken some post-transfer efforts to vindicate Pioneer's position in this regard,[31] does not represent the kind of error or mistake that would give rise to bank liability in conversion for wrongful setoff. *Cf.* 2 CLARK, THE LAW OF SECURED TRANSACTIONS §7.08[2][b] (noting that the bailee-with-notice concept does not eliminate the risk that an investor will tender payment to a loan originator as opposed to the warehouse lender).[32]

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[31] Pioneer presented evidence that, acting at Pioneer's behest, Norwest personnel did at one point make an ineffectual attempt to reverse the transfers as mistaken, although Norwest representatives maintained the position throughout trial that the transfers occurred in due course, according to the instructions of its business correspondent, AFMC.

[32] Parenthetically, we note that such considerations would not likely relieve various other parties to the transaction from liability to

(Continued on following page)

Having considered these and other facets of the case, we conclude that a new trial is not implicated.[33]

Finally, we observe that CoreStates has raised a number of other important legal issues in this appeal. Most significantly, the framing of the case in terms of Article 4A of the Uniform Commercial Code and the incorporating provisions of Federal Reserve Board Regulation J, 12 C.F.R. 210.25(a), (b), governing fund transfers, has attracted the attention of multiple *amici,* including the Federal Reserve Banks. In this regard, CoreStates has maintained throughout the litigation that Article 4A's express authorization of bank setoff, *see* 13 Pa.C.S. §4A502(c) (providing, *inter alia,* that "the amount credited [via wire transfer] may be set off against an obligation owed by the beneficiary to the bank"), as incorporated into Regulation J, preempts common law distinctions based on ownership or secured status external to Article 4A as they might otherwise pertain to the lawfulness of bank setoff. In this regard, CoreStates' position appears to encompass the assertion that the *Sherts* holding has been preempted (or at least substantially displaced) by statute. This, in

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Pioneer, including Norwest (which settled with Pioneer and whose ability to retain the collateral free and clear of Pioneer's interest would likely have depended, at least in part, on its prior knowledge of that interest, *see* 13 Pa.C.S. §§3302, 3306), AFMC and Flatley (who suffered judgment at trial), or RNG's principal (who had executed a personal guarantee in favor of Pioneer).

[33] In light of our holding with respect to CoreStates' liability on the underlying cause of action for conversion, a new trial with respect to the issue of punitive damages is also not warranted. *See Kirkbride v. Lisbon Contractors, Inc.,* 521 Pa. 97, 101, 555 A.2d 800, 802 (1989) ("If no cause of action exists, then no independent action exists for a claim of punitive damage[s] since punitive damages [are] only an element of damages." (emphasis deleted)).

turn, has given rise to concerns on the part of another *amicus,* whose interests are representative of a substantial body of persons and organizations that are beneficiaries of statutory trusts arising by operation of federal law, for example, in proceeds from the sale of perishable agricultural commodities. *See* 7 U.S.C. §499e(c). This *amicus* presents the counter argument that Article 4A's setoff provision was intended to incorporate existing setoff and priority rules into the funds transfer arena, not to supplant them. Given our determination, above, however, there is simply is no conflict between Article 4A (or Regulation J) and Pennsylvania common law concerning any material point of the present dispute. Therefore, although we acknowledge the importance of this issue and the respective merits of the competing positions, according to the general principles by which we address controversies, resolution will be reserved for a case in which the question would be of controlling significance.[34]

The order of the Superior Court is reversed and the matter is remanded for entry of judgment notwithstanding the verdict in favor of CoreStates.

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[34] Similarly, the parties' arguments frame a respectable debate regarding the scope of Pennsylvania's adverse claims statute, 7 Pa.C.S. §606, according to the respective positions articulated by the Superior Court majority and dissent set forth in *E.F. Houghton & Co. v. Doe,* 427 Pa. Super. 303, 628 A.2d 1172 (1993).

Madame Justice Newman did not participate in the consideration or decision of this case.

Judgment entered
Dated: August 19, 2004

/s/ John W. Person, Jr.
John W. Person, Jr., Esquire
Deputy Prothonotary

IN THE SUPREME COURT OF PENNSYLVANIA
EASTERN DISTRICT

PIONEER COMMERCIAL FUNDING CORP. AND BANK ONE, TEXAS, N.A.,	:	
v.	:	No. 279 EAL 2002
AMERICAN FINANCIAL MORTGAGE CORPORATION, THOMAS F. FLATLEY, NORWEST FUNDING, INC., AND CORESTATES BANK, N.A.,	:	Petition for Allowance of Appeal from the order of the Superior Court
PETITION OF: CORESTATES BANK, N.A.	:	

ORDER

PER CURIAM

AND NOW, this 2nd day of December, 2003, the Petition for Allowance of Appeal is **GRANTED**, limited to the following issues:

1. Whether an action for conversion can be used to circumvent Section 4A502 of the UCC, 13 Pa.C.S. § 4A205; and, if so, whether CoreStates satisfied the common-law elements for a valid setoff.

2. Whether Pioneer should have acted pursuant to the adverse claim statute, as set forth in Section 606 of the Banking Code.

3. Whether consequential damages are available for a wrongful setoff.

4. Whether punitive damages were available in this case.

5. Whether Pioneer lack [sic] a valid security interest in the funds.

The Application by Petitioner for Leave to Permit Prothonotary to Distribute Clarifying Letter to the Court filed on December 30, 2002 is **GRANTED**. Also, the Application by Petitioner for Leave to Permit Prothonotary to Distribute Clarifying Letter to the Court filed on August 9, 2002 and the Application for Leave to Permit Prothonotary to Distribute the Attached Opinion to the Court are **DENIED**.

Mr. Justice William H. Lamb did not participate in the consideration or decision of this matter.

J-A38041-01

2002 PA Super 68

PIONEER COMMERCIAL FUNDING CORP. AND BANK ONE, TEXAS, N.A.	:	IN THE SUPERIOR COURT OF PENNSYLVANIA
v.	:	
AMERICAN FINANCIAL MORTGAGE CORP., THOMAS F. FLATLEY, NORTHWEST FUNDING, INC. AND CORESTATES BANK, N.A.	:	
APPEAL OF: CORESTATES BANK, N.A.	:	No. 144 EDA 2001

Appeal from the Judgment entered December 21, 2000, In the Court of Common Pleas of Philadelphia County, Civil Division at No. 885 April Term 1998.

BEFORE: JOHNSON, JOYCE AND BECK, JJ.

OPINION BY JOYCE, J: Filed March 18, 2002.

¶ 1 Appellant, CoreStates Bank, N.A. (Bank),[1] appeals from the judgment entered by the trial court on December 21, 2000,[2] following a jury verdict in favor of Appellee,

[1] CoreStates Bank was acquired by First Union National Bank in April 1998. The parties stipulated that all claims and defenses of CoreStates would apply to First Union. Thus, we will refer to both First Union and CoreStates collectively as the "Bank."

[2] Although the judgment was entered on the docket on December 20, 2000, pursuant to Pa.R.C.P. 236, notice of the order was sent to the parties on December 21, 2000. *See* Pa.R.A.P. 108(b) (the date of entry of an order in a matter subject to the Pennsylvania Rules of Civil Procedure shall be the day on which the clerk makes the notation on the docket that notice of entry of the order has been given as required by

(Continued on following page)

Pioneer Commercial Funding Corporation (Pioneer). For the reasons set forth herein, we affirm in part and reverse in part.

¶ 2 The pertinent facts and procedural history of this case are as follows. Appellee, Pioneer, is a mortgage funding company, a warehouse lender. Pioneer had a business relationship with RNG Mortgage Services, Inc. (RNG), a California-based mortgage banker. A May 1997 agreement governing the business relationship provided that Pioneer would receive a security interest in the notes and mortgages obtained by RNG (the collateral) and in any proceeds of the notes and mortgages. In order to protect Pioneer's interest in the notes, RNG ordinarily would endorse the notes in blank and deliver them to Pioneer, which in turn, delivered the notes to Bank One, Texas (Bank One). Bank One would then send the individual notes under bailee letters,[3] releasing them from its custody as they were paid by the ultimate secondary-market investors that purchased them. RNG "originated" mortgages, i.e., loaned money to home buyers and sold the resulting notes and mortgages to investors such as Pioneer. As a warehouse lender, Pioneer advanced money to RNG so that RNG could fund loans to homebuyers. On its part, Pioneer derived its funding from Bank One.

¶ 3 In August 1997, RNG filed for bankruptcy pursuant to Chapter 11 of the Bankruptcy Code. American Financial

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Pa.R.C.P. 236(b)). Pa.R.C.P. 236 provides that the prothonotary shall immediately give written notice of the entry of any order, decree or judgment to each party's attorney of record.

[3] A bailee letter is a legal mechanism that allows a secured creditor to release possession of a negotiable instrument such as a note, without losing the perfected status of its interest in the collateral.

Mortgage Corporation (AFMC), a mortgage originator, upon learning of RNG's bankruptcy, entered into negotiations to acquire RNG. AFMC then persuaded Pioneer to continue its funding of RNG's consumer loans so as to keep open RNG's pipeline of unfunded mortgage commitments. Pioneer, RNG, and AFMC then entered into a loan and security agreement, with Pioneer as the lender and AFMC as the borrower. Thomas Flatley, AFMC's principal, guaranteed AFMC's obligations under the agreement. Under the agreement, Pioneer would continue funding RNG's loans as long as RNG was able to locate investors to purchase them. RNG and AFMC then obtained commitments from Norwest Funding, Inc. (Norwest). The commitments meant that Norwest would purchase the RNG loans that Pioneer funded. Due to the fact that RNG was in bankruptcy, as a condition for its commitments, Norwest insisted that AFMC guarantee the performance of the homeowners on the underlying notes, which AFMC did. The net effect of this complex arrangement is that the notes would be sent from Bank One to AFMC under a bailee letter; AFMC would endorse the notes and send them along with the bailee letter to Norwest; and Norwest would then wire the funds directly to Pioneer's account at Bank One. Norwest was given wiring instructions to wire the funds to Pioneer's account at Bank One.

The First Transaction (The First Portfolo):

¶ 4 Pursuant to this elaborate and complex arrangement, RNG obtained notes from title companies, endorsed them in blank and sent them to Pioneer. Pioneer then sent the notes to Bank One. Bank One later sent the notes, along

with the bailee letter[4] to AFMC. Upon receiving these items, AFMC endorsed the notes and sent them, along with other documents to Norwest, Norwest having previously agreed to purchase approximately $2.3 million worth of RNG-originated loans (First Loan Portfolio). Norwest then inspected the notes and wired approximately $2.1 million to AFMC's account at the Bank. This wire transfer took place on November 4, 1997. Norwest wired the funds to AFMC's account despite the parties' agreement and understanding that the funds should be wired directly to Pioneer's account at Bank One. Shortly after learning that Norwest did not wire the funds to the expected account, an official of RNG, Melanie Hotz, and Glenda Klein of Pioneer, quickly informed AFMC of this situation. As a result, AFMC requested the Bank to wire the funds to Pioneer's account at Bank One. The Bank promptly complied with AFMC's request and wired the funds to Bank One.

The Second Transaction (The Second Portfolio):

¶ 5 Again, pursuant to the parties' arrangement, the second loan transaction proceeded like the first one. At a

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[4] The bailee letter stated as follows: "The enclosed notes . . . and other documents ("collateral") . . . have been assigned and pledged to (a) Pioneer Commercial Funding Corp., ("borrower") as collateral under a loan and security agreement. . . . The collateral is being delivered to you for a purchase under the existing take out commitment. . . . Either payment in full for the collateral or the collateral itself must be received within 45 days after the date of this letter. Until that time you are deemed to be holding the collateral in trust, subject to the security interest granted first to borrower and then to agent for lenders and as agent's bailee in accordance with the applicable provisions of the Uniform Commercial Code. . . . Payment for collateral must be made by wire transfer or immediately available funds to: Bank One, Texas N.A., agent account . . . credit: Pioneer Commercial Funding Corp. . . . "

later stage of the transaction, AFMC sent the notes to Norwest. Prior to this second transaction, representatives of RNG, Pioneer and AFMC contacted Norwest to ensure that the payments would be sent to Pioneer's account at Bank One rather than AFMC's account at the Bank. Despite the instructions to the contrary, AFMC, of its own accord, later sent wiring instructions to Norwest to wire the funds to AFMC's account at the Bank.

¶ 6 On November 12, 1997, Norwest wired $1,454,699.80 to AFMC's account at the Bank. Norwest subsequently wired other funds to the above account on two other occasions: November 13, 1997 ($209,984.33), and November 19, 1997 ($114,835.86). The amounts wired by Norwest to AFMC's account at the Bank totaled $1,779,519.99 (the Fund). Part of this amount was the remaining payment for the First Portfolio while the remainder was applied to the payment for the Second Portfolio.

¶ 7 Unbeknownst to Pioneer, RNG, and Bank One, AFMC had become indebted to the Bank in excess of $4 million through overdrafts. On November 6, 1997 the Bank imposed a debit restraint on all the accounts of AFMC and its affiliates, meaning that AFMC and its affiliates could deposit but could not withdraw funds from these accounts.

¶ 8 On November 25, 1997, AFMC notified the Bank that Norwest had wrongly deposited $1,779,519.99 (the Fund) into AFMC's account at the Bank. Norwest also requested the Bank to reverse the wire transfers sent to AFMC's account. Despite these notifications, the Bank claimed that it had already exercised its right to setoff the amount deposited into AFMC's account against the amount owed by AFMC through overdrafts. The Bank and Thomas

Flatley of AFMC subsequently entered into a workout agreement under which the Bank would retain the money deposited by Norwest. Pioneer was not informed of this agreement. Pioneer then sought to recover the money from the Bank, claiming that Norwest deposited the money into AFMC's account in error.

¶ 9 Following the Bank's refusal to forward the Fund to Pioneer upon request, on April 20, 1998, Pioneer initiated this action through the filing of a complaint alleging that the Bank committed the tort of conversion. The named defendants were the Bank, AFMC, Thomas F. Flatley, and Norwest. The case proceeded to a jury trial on June 2, 2000. The trial was conducted in a bifurcated fashion consisting of the liability phase followed by the damages phase. On July 26, 2000, after deliberation, the jury found the Bank liable for conversion and returned a verdict in favor of Pioneer in the following amounts: $1,779,519.99 (compensatory damages), $13.5 million (consequential damages) and $337.5 million (punitive damages).

¶ 10 On August 28, 2000, the Bank filed post-trial motions seeking judgment notwithstanding the verdict (JNOV) and a new trial or remittitur. On December 4, 2000, the trial court denied the Bank's motion for JNOV and for a new trial. The trial court however, granted the remittitur, reducing the punitive damages to $40.5 million. On December 21, 2000, after including the interest on the compensatory damages award, the trial court entered judgment in favor of Pioneer in the amount of $55,858,374.28. On January 3, 2001, the Bank timely appealed to this Court, raising the following issues:

> 1. When funds (proceeds from the sale of notes) are wired to a depositor's unrestricted bank account, is the bank's right to set off the funds

against the depositor's uncontested debt to the bank superior to that of a claimant asserting a security interest in the proceeds where: (a) the claimant failed to comply with the requirements for obtaining a valid security interest; (b) the purchaser intended to and did wire the payment in the proper amount to the depositor, who was entitled to receive it; (c) the depositor had been purposefully interposed in the chain of title of the notes; and (d) the claimant failed to comply with Pennsylvania's adverse claims statute?

2. Is a new trial required because the court: (a) failed to instruct the jury that setoff occurs by operation of law and that it takes priority over a security interest; (b) allowed the claimant to portray the bank's exercise of the setoff and subsequent execution of a workout agreement with the depositor as a conspiracy; (c) sanctioned the bank for discovery violations by allowing the claimant to parade the discovery disputes before the jury, while barring the bank's former counsel from testifying about the discovery disputes and the workout agreement; and (d) permitted a wide range of inflammatory statements to be made to the jury?

3. May a claimant recover consequential damages for wrongful setoff by a bank, and, if so, were the plaintiff's damages proximately caused by the setoff and measured in a manner permitted by Pennsylvania law?

4. Is the bank subject to punitive damages even though (a) statutory common law supported its position and (b) it acted on the advice of counsel?

5. Was the $40.5 million remitted punitive award excessive under the Due Process Clause

> and Pennsylvania law, and did the trial court err in admitting evidence of the net worth of the parent of the bank's merger partner for purposes of determining punitive damages?

Bank's Brief, at 2.

¶ 11 Since many of the issues raised by the Bank stem from the denial of post-trial motions seeking judgment notwithstanding the verdict and/or a new trial, we begin by setting forth the governing standards of review.

> The decision whether to grant a new trial lies within the trial court's discretion. ***Martin v. Evans,*** 551 Pa. 496, 501-02, 711 A.2d 458, 461 (1998). Therefore, when reviewing an order denying a motion for a new trial, we must determine whether the trial court "clearly and palpably abused its discretion or committed an error of law which affected the outcome of the case." ***Whyte v. Robinson,*** 421 Pa.Super. 33, 617 A.2d 380, 382 (1992). "A new trial is warranted when the jury's verdict is so contrary to the evidence that it shocks one's sense of justice." ***Martin,*** 551 Pa. at 501, 711 A.2d at 461. Conversely, JNOV may be entered if, after considering only the evidence supporting the verdict and giving the verdict winner the benefit of the doubt, the trial court clearly finds that the movant is entitled to judgment as a matter of law, and the evidence presented at trial was such that no two reasonable minds could disagree that the verdict should be in favor of the movant.[5] ***Degenhardt v.***

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[5] Put differently, there are two bases upon which a judgment n.o.v. can be entered: one, the movant is entitled to judgment as a matter of law, and/or two, the evidence was such that no two reasonable minds could disagree that the outcome should have been rendered in favor of

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> ***Dillon Co.,*** 543 Pa. 146, 153, 669 A.2d 946, 950 (1996). Finally, we note that credibility determinations are for the jury, which "is entitled to believe all, part, or none of the evidence presented. ***Randt v. Abex Corp.,*** 448 Pa. Super. 224, 671 A.2d 228, 233 (1996)."

Brinich v. Jencka, 757 A.2d 388, 395 (Pa. Super. 2000).

¶ 12 Some issues raised by Appellant involve challenges to the trial court's conclusions of law. As such our review of these issues is plenary. ***See Moorhead v. Crozer Chester Med. Ctr.,*** 765 A.2d 786, 788 (Pa. 2001); ***Phillips v. A-Best Products Co.,*** 665 A.2d 1167, 1170 (Pa. 1995). ***See also American Appliance v. E.W. Real Estate Management, Inc.,*** 769 A.2d 444, 446 (Pa. 2001) (appellate review of questions of law is plenary).

Sufficiency of the Evidence: Conversion:

¶ 13 "Conversion is the deprivation of another's right of property in, or use or possession of, a chattel, without the owner's consent and without lawful justification." ***Shonberger v. Oswell,*** 530 A.2d 112, 114 (Pa Super. 1987). According to ***L.B. Foster Co. v. Charles Caracciolo Steel & Metal Yard, Inc.,*** 777 A.2d 1090, 1095-1096 (Pa. Super. 2001),

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the movant. With the first, a court reviews the record and concludes that even with all factual inferences decided adverse to the movant the law nonetheless requires a verdict in his favor, whereas with the second the court reviews the evidentiary record and concludes that the evidence was such that a verdict for the movant was beyond peradventure. ***Moure v. Raeuchle,*** 604 A.2d 1003, 1007 (1992) (citations omitted).

> the classic definition of conversion under Pennsylvania law is the deprivation of another's right of property in, or use or possession of, a chattel, or other interference therewith, without the owner's consent and without lawful justification. Although the exercise of control over the chattel must be intentional, the tort of conversion does not rest on proof of specific intent to commit a wrong. It is fundamental that a good faith purchaser of goods from a converter is also a converter and must answer in damages to the true owner. The general rule for chattels is that "a bona fide purchaser from a thief gets nothing." This is so because a converter has no title to the chattels, and thus can convey nothing to a bona fide purchaser for value.

Id. (citations and quotation marks omitted).

¶ 14 It must also be noted that money may be the subject of conversion. ***Shonberger v. Oswell, supra,*** 530 A.2d at 114. Since Pioneer's complaint alleged that the Bank committed the tort of conversion with respect to the Fund, as a threshold matter, we must determine whether Pioneer established that it had a property right with respect to the Fund at the time of the alleged conversion. It is only after it is determined that one has a property right in a chattel that an inquiry must be made as to whether there has been a deprivation of, or an interference with that right to constitute conversion.

¶ 15 Viewed in the light most favorable to Pioneer, as the verdict winner, there was sufficient evidence to support the jury's determination that Pioneer owned the Fund and that the Bank was liable for conversion. Melanie Hotz (RNG), Glenda Klein (Pioneer), Howard Seidman (AFMC), and Joseph Scheuren (AFMC) all testified that the Fund

belonged to Pioneer. In addition to the testimony of the above individuals, the notes which generated the Fund were accompanied by bailee letters which indicated that Pioneer and Bank One owned the notes and the proceeds of the notes. Also, shortly after the Fund was wired to AFMC's account at the Bank, Pioneer and Norwest notified the Bank that the Fund did not belong to AFMC but to Pioneer; and David Moffitt, counsel for AFMC, also notified the Bank in writing that the Fund belonged to Pioneer. Additionally, we note that when the proceeds of the First Portfolio were wired to AFMC's account at the Bank, the Bank was promptly notified that the money did not belong to AFMC but to Pioneer. Without much ado, the Bank permitted the money to be wired to Pioneer's account with Bank One Texas. Given what occurred with the proceeds of the First Portfolio, the testimony of the participants in the transactions, the bailee letters and other documentary evidence, we conclude that sufficient evidence was adduced at trial to support the jury's finding that the Fund belonged to Pioneer.

Applicability of the Bankruptcy Code:

¶ 16 The Bank argues that under the Bankruptcy Code, the filing of a bankruptcy petition extinguished all pre-petition grants of security interests as to property acquired post petition. 11 U.S.C. § 552(a). The Bank maintains that since RNG filed its bankruptcy petition in August 1997, and the First and Second Portfolios contained loans made by RNG in October and November 1997 (post-petition loans), these loans cannot be subject to the security interest created by the May 1997 agreement (pre-petition agreement). The Bank's recitation of the general provisions of section 552(a) is correct. This

section, however, does not afford Bank any relief. The Bank is correct that under 11 U.S.C. § 364(c), a bankruptcy trustee/debtor-in-possession must receive court approval before obtaining credit or incurring a debt secured by lien. Section 364(c) allows the bankruptcy court, after notice and a hearing, to authorize the incurring of debt and the granting to creditors of either (1) priority over all other administrative expenses, (2) a lien on property of the estate not otherwise subject to a lien, or (3) a junior lien on property of the estate subject to a lien. Pursuant to the above section, in trustee-debtor versus creditor disputes, bankruptcy courts have routinely held that a creditor who purports to extend secured credit to a bankruptcy trustee without court approval is not entitled to priority or super-priority treatment. ***See e.g. In re Pizza of Hawaii, Inc.,*** 69 B.R. 60 (Bkrtcy. D. Hawaii 1986) (Creditor did not have priority administrative claim where loan occurred post-petition, and no hearing was held to authorize incurring of debt). However, bankruptcy courts do not **automatically** rescind or strip post-petition "secured" debts (obtained without court approval) of their secured status simply because there was no prior court approval. Some courts have exercised their discretion in deciding the remedy for the failure to obtain court approval. ***See e.g. In re McConville,*** 110 F.3d 47 (9th Cir. Cal. 1997), *certiorari denied* 118 S.Ct. 412, 522 U.S. 966, 139 L.Ed.2d 315 (The appropriate remedy, when Chapter 11 debtors-in-possession unlawfully executed deed post-petition, without first obtaining bankruptcy court approval of their ability to incur secured post-petition debt, was order limiting amount of deed of trust lien and not totally rescinding deed of trust, where loan advanced by deed of trust lenders had enabled debtors to obtain deed of trust property for benefit of estate; however, in light of lenders

failure to make any inquiry as to debtors' financial condition prior to making post-petition loan, lenders were entitled to lien in deed of trust property only for unreimbursed portion of funds which they blindly advanced, with no benefit from loan).

¶ 17 In the case at bar, RNG's failure to obtain bankruptcy court approval before obtaining a secured loan from Pioneer did not **automatically** strip the loan of its secured status. However, the bankruptcy court, upon petition by a party with standing to do so, could rescind the transaction and/or strip the loan of its secured status. In the case of RNG, there has been no petition to the bankruptcy court to strip the loan of its secured status, and the bankruptcy court has not ruled that the loan must lose its secured status because of RNG's failure to obtain court approval before obtaining the loan from Pioneer. Therefore, we cannot agree with the Bank that Pioneer's loan to RNG was a general, unsecured loan and that Pioneer was nothing more than a general, unsecured creditor of RNG. Consequently, Pioneer had at least, a security interest in the Fund. Thus, the Bankruptcy Code affords Bank no relief. Parenthetically, we question the Bank's standing to raise issues related to RNG's bankruptcy case: the Bank was not a creditor to RNG; the Bank was not involved in a transaction with RNG either pre- or post-petition; and the Bank was not otherwise involved in the bankruptcy proceedings. As Pioneer correctly pointed out, no court has ever invalidated a creditor's security interest when the complaining party was not a party to the bankruptcy case, was not otherwise involved in the bankruptcy proceeding and has not petitioned the bankruptcy court to invalidate the security interest at issue. In essence, the Bank invites us to be the first court to invalidate a security interest in a

loan obtained without bankruptcy court approval even though the complainant was not involved in the bankruptcy proceeding and has not petitioned the bankruptcy court to invalidate the security interest. We politely decline this invitation.[6]

Applicability of Section 4A502 of the UCC:

¶ 18 The Bank argues that even if Pioneer had a valid security interest in the Fund, the Bank is entitled to judgment pursuant to 13 Pa.C.S.A. § 4A502(c). Section 4A502(c) provides that:

> **(c) Payment orders issued to beneficiary's bank.** – If a beneficiary's bank has received a payment order for payment to the beneficiary's account in the bank, the following rules apply:
>
> (1) The bank may credit the beneficiary's account. The amount credited may be set off against an obligation owed by the beneficiary to the bank or may be applied to satisfy creditor process served on the bank with respect to the account.
>
> (2) The bank may credit the beneficiary's account and allow withdrawal of the amount credited unless creditor process with respect

[6] Although the trial court incorrectly suggested that Pioneer's secured loan to RNG was made in the ordinary course of business, and, therefore, needed no bankruptcy court approval, we affirm, albeit on different grounds, the trial court's conclusion that the Bankruptcy Code does not mandate the invalidation of Pioneer's security interest despite the absence of bankruptcy court approval. ***See Lobianco v. Property Protection, Inc.***, 437 A.2d 417, 424 (Pa. Super. 1981) (an appellate court may affirm the decision of the trial if it is correct on any grounds).

to the account is served at a time and in a manner affording the bank a reasonable opportunity to act to prevent withdrawal.

(3) If creditor process with respect to the beneficiary's account has been served and the bank has had a reasonable opportunity to act on it, the bank may not reject the payment order except for a reason unrelated to the service of process.

¶ 19 The Bank argues that pursuant to section 4A502(c)(1), when the Fund was wired to AFMC's account, the Bank automatically effectuated a setoff of that amount and applied it to AFMC's debt to the Bank. According to the Bank, the setoff occurred automatically and not on December 18, 1997 as the trial court opined.

¶ 20 We agree with the Bank that pursuant to ***Royal Bank of Pennsylvania v. Selig,*** 644 A.2d 741 (Pa. Super. 1994), it had an automatic right of setoff and need not take any affirmative steps to effectuate this right. "Set-off, however, is appropriate only where certain conditions are met. There must be mutuality of obligation between the bank and the depositor; the funds against which set-off is exercised must belong to the depositor; the funds must be deposited with the bank into a general account; and, the debt owed by the depositor to the bank must be mature." ***Id.*** at 744 (citations omitted).

¶ 21 In the instant case, it is undisputed that the debt owed by AFMC (the depositor) to the Bank was mature at the time the Fund was wired into AFMC's account and that there was a mutuality of obligation between the Bank and AFMC. Further, the jury determined that AFMC's account with the Bank was a general account. Thus, it would appear that the Bank has met most of the

conditions for exercising its right of automatic setoff. However, a critical element of the right to automatic setoff is that the funds against which setoff is exercised must belong to the depositor. On this issue, the jury unequivocally found that Pioneer had an ownership interest in the Fund wired to AFMC's account with the Bank. Since the jury determined that the Fund belonged to Pioneer and not to AFMC, the Bank could not exercise its right of automatic setoff against the Fund.

¶ 22 The Bank strenuously argues that the UCC, specifically, 13 Pa.C.S.A. § 4A502 de-emphasizes ownership, eliminating the requirement that the funds against which setoff is exercised must belong to the depositor. We disagree. Nothing in the language of section 4A502 or in Pennsylvania case law indicates or mandates that a Bank should not determine whether the funds belong to a depositor before setoff is exercised. Indeed, if the ownership requirement were eliminated, it would lead to the absurd consequence whereby a Bank could effectuate an automatic setoff even when funds are mistakenly or inadvertently wired or deposited to the wrong account. We are therefore not persuaded by the Bank's argument that the issue of the ownership of the Fund is irrelevant under 13 Pa.C.S.A. § 4A502

¶ 23 Interestingly, in another section of its brief, (Bank's Brief, at 24), the Bank argues that the evidence established that AFMC owned the Fund and that as a result, the Bank met all the requirements for an automatic setoff. We must point out that this argument which emphasizes AFMC's alleged ownership of the Fund is inconsistent with the Bank's argument (bank's Brief, at 20-21) that ownership of the Fund is irrelevant under the UCC. As we previously pointed out, the jury found, based on ample

evidence, that Pioneer owned the Fund. Therefore, the Bank's assertion that AFMC owned the Fund must fail.

¶ 24 The next argument advanced by the Bank is that the trial court committed an error of law in its jury instructions. The Bank cited the following portion of the jury instruction:

> Now, a bank has a right under the law to freeze an account, a debit account, for purposes of collecting a debt from the depositor under limited circumstances. One the debt must be mature. Well under the circumstances of this case the debt was mature. AFMC owed the money to CoreStates for the overdrafts.
>
> The other condition is that the money must belong to AFMC. So it must be known that CoreStates is able to seize. That's a jury issue that you're going to answer: Was it AFMC's money, or was there a security interest in plaintiff, in this case Pioneer Commercial Funding?
>
> * * *
>
> You have to decide * * * if, one, that these funds belonged to Pioneer as a secured creditor, which is a superior right than an unsecured creditor, as I discussed with you. You have to make that decision. And in Question Number One, that says: Do you find that the plaintiff had this ownership interest about which I discussed with you which would have entitled them to the funds [?] the answer would be yes or no.

Bank's Brief, at 30-31.

¶ 25 The Bank interpreted the above instructions to mean that "if Pioneer was a secured creditor, CoreStates

[the Bank] had an obligation to release the Fund." ***Id.*** at 32.

> When examining jury instructions, our scope of review is to determine whether the trial court committed clear abuse of discretion or error of law controlling the outcome of the case. Error in a charge is sufficient ground for a new trial, if the charge as a whole is inadequate or not clear or has a tendency to mislead or confuse rather than clarify a material issue. A charge will be found adequate unless the issues are not made clear to the jury or the jury was palpably misled by what the trial judge said or unless there is an omission in the charge which amounts to fundamental error. When reviewing a charge to the jury, we will not take the challenged words or passage out of context of the whole of the charge, but must look to the charge in its entirety.

Bannar v. Miller, 701 A.2d 232, 240 (Pa. Super. 1997) (citations and quotation marks omitted).

¶ 26 Reviewing the Bank's argument in light of the above standards, we find the trial court did not commit an error of law. After reviewing the trial court's jury instructions in their entirety, we find that the trial court properly instructed the jury that it is their responsibility to determine whether Pioneer had an ownership interest in the Fund and that it is only if it is determined that Pioneer had a property interest in the Fund that Pioneer can maintain an action for conversion. We refuse to isolate certain phrases and passages from the trial court's jury instruction and interpret them out of context as the Bank does in its argument. Further the Bank suggests that the following instruction may have palpably misled the jury: "A jury issue you're going to answer [is]: Was it AFMC's

money, or was there a security interest in plaintiff, in this case Pioneer Commercial Funding?" The jury was not misled by the above instruction and did not confuse any interests which AFMC may have had in the Fund with Pioneer's interest. The jury's understanding was clearly shown in its affirmative answer to following question: "Do you find that plaintiff Pioneer Commercial Funding Corporation had an ownership interest in the funds wired by Norwest to American Financial Mortgage Corporation's settlement account at defendant CoreStates Bank that entitled plaintiff to possession of the funds?" Accordingly, we find no defect in the jury instructions sufficient to warrant a new trial.

Applicability of the Banking Code:

¶ 27 Another issue raised by the Bank relates to the applicability of the Pennsylvania Adverse Claims Statute (Section 606 of the Banking Code of 1965, 7 P.S. § 606). The Bank maintains that it is entitled to a directed verdict because it had a statutory defense to Pioneer's conversion claim, namely, Pioneer's failure to assert a claim to the Fund pursuant to the adverse claims statute. Relying on Section 606(b), the Bank argues that Pioneer, as the party seeking to make an adverse claim, was required to either obtain a declaratory judgment in support of its right of ownership or post a bond. According to the Bank, because Pioneer failed to meet these two requirements, Pioneer's conversion must fail. After reviewing the record and the applicable law, we must disagree with the Bank's position. As Pioneer correctly points out, the Pennsylvania Adverse Claims Statute applies to claims by a third party adverse to the claim of a depositor. The comment to Section 606 indicates that the purpose of the statute is to limit the

involvement of banks in disputes between depositors and third parties. In the case at bar, Pioneer's claim to the Fund is not adverse to that of the depositor, AFMC. Indeed, at the outset, AFMC unequivocally disclaimed any interest in the Fund, and told the Bank that the Fund belonged to Pioneer. Thus, the issues involved in this case do not implicate the adverse claims statute.

¶ 28 Both Pioneer and the Bank cite to different parts of our Court's decision in ***E.F. Houghton & Co. v. Doe,*** 627 A.2d 1172 (Pa. Super. 1993) in support of their respective positions regarding the applicability of Section 606 of the Banking Code. In ***Houghton,*** we addressed the issue of the nature of the notice that must be given to a bank by a third party under Section 606 of the Banking Code in order for the third party to assert successfully a claim to funds in a depositor's account superior to that of the depositor or the bank itself. The relevant facts of ***Houghton*** are as follows: An employee of E.F. Houghton & Company (Houghton) stole about $1,000,000 from Houghton and deposited the money into two accounts at Mellon Bank. The two accounts were in the name of the Houghton employee, Bruno, and his wife. Using the $1,000,000 as collateral, Mellon Bank approved a $150,000 loan to Bruno and his wife. One of the terms of the loan agreement was that in the event of default, Mellon Bank was entitled to withdraw $150,000 plus accrued interest from the Brunos' accounts to pay the debt. Houghton later discovered Bruno's theft and subsequently obtained judgment against the Brunos. Houghton then notified Mellon Bank in writing regarding the theft. Houghton also requested Mellon Bank to freeze the funds in the accounts. Upon Mellon Bank's refusal to freeze the account without a court order, Houghton then obtained a writ of attachment.

Before receiving the writ of attachment, Mellon Bank, withdrew from one of the Brunos' accounts the sum of $151,481.88 representing the principal and interest on its loan to the Brunos, the Brunos having defaulted on th[illegible] payments. On appeal, Houghton relied on ***Sherts v. Fulton Nat'l Bank,*** 21 A.2d 18 (Pa. 1941)[7] and argued that Mellon Bank's setoff prior to service of the writ of attachment was an illegal conversion. Houghton argued that "if a bank has knowledge, or notice of facts enough to put it upon inquiry, that the funds in a depositor's account actually belong to a third person, it may not apply such funds to a debt owed to it by the depositor individually." ***Id.*** at 1175, citing ***Sherts.***

¶ 29 In rejecting Houghton's argument our Court distinguished ***Houghton*** from ***Sherts,*** noting that "Sherts had not attempted to mislead the bank as to the true ownership of the funds, and that the bank therefore could not avoid treating it as money held in trust for Sherts' client. The claims asserted by Sherts' clients against the bank were not "adverse" to Sherts himself, as he never pretended that the money was his own." ***Id.*** at 1175. We also noted that in ***Houghton,*** unlike ***Sherts,*** Mellon Bank relied on the representations of the depositors who affirmatively misled the bank into believing that certain

[7] In ***Sherts,*** the depositor, Sherts, who is an attorney, maintained a checking account in the bank in his individual name and subsequently, added the word "attorney" to the name in the passbook and on the bank's ledger sheets. Thereafter, he placed only collections made for clients in the account, and signed all checks as "attorney." He also maintained another account in the name "H. Edgar Sherts, Farm Account," in which he held funds for a decedent's estate. The bank later applied the balances in both accounts toward the payment of an overdue note owed by Sherts personally to the bank.

stolen funds actually belonged to them. ***Id.*** at 1176. Also, unlike ***Sherts,*** the ***Houghton*** appeal did not involve deposit funds held for the benefit of a third party, in a trust, fiduciary or agency context. ***Id.*** at 1175-1176.

¶ 30 Based on our careful review of ***Houghton,*** we agree with Pioneer that ***Houghton*** is distinguishable from the instant case. In ***Houghton,*** the Brunos claimed an interest in the funds. Houghton's claim to the funds was therefore adverse to the Brunos' interest. In the instant case, however, Pioneer's claim to the Fund is not adverse to the depositor, AFMC. Shortly after the wire transfer, AFMC promptly disclaimed any interest in the Fund and notified the Bank that the Fund belonged to Pioneer. Also, when the above facts are considered in conjunction with the bailee letters, which accompanied the notes in this case, it is clear that the notes and the proceeds of the notes were being held in trust or for the benefit of Pioneer and Bank One. The Funds never belonged to AFMC. Thus, similar to ***Sherts,*** the Fund in this case was deposited into AFMC's account for the benefit of a third party, and the owner of the account, AFMC disclaimed any interest in the Fund. Based on the foregoing analysis, we hold that the Bank is not entitled to relief pursuant to Section 606 of the Banking Code.

The Trial Judge's Conduct at the Trial:

¶ 31 *Allegations of conspiracy.* The Bank argues that the trial court improperly permitted Pioneer to make inflammatory allegations that the Bank was guilty of conspiracy and cover-up, based on the Workout Agreement between the Bank and AFMC, even though the complaint never set forth a claim for conspiracy. We agree with the Bank that

the trial court erroneously permitted Pioneer to make allegations of conspiracy and cover-up during the trial. However, this error is harmless with respect to the liability verdict because the jury did not find the Bank liable for conspiracy and the verdict slip did not contain the conspiracy charge and the jury did not return a verdict on the issue of conspiracy. The jury returned a verdict on the issue of conversion. ***See Bannar v. Miller,*** 701 A.2d 232, 241-242 (Pa. Super. 1997) (where the trial court erroneously charged the jury on civil conspiracy even though plaintiff had withdrawn the conspiracy count of the complaint, the error was harmless because conspiracy was not reflected on the verdict slip, and the jury was incapable of returning a verdict on that count). In the instant case, with respect to the liability, the trial court's error was less egregious because the trial court, unlike in ***Bannar,*** did not instruct the jury on the issue of conspiracy. Thus, any error which the trial court may have committed in permitting allegations of conspiracy and cover-up is harmless with respect the finding of liability.[8] Apart from these allegations of conspiracy and cover-up, sufficient evidence was adduced to support the jury's verdict on the issue of conversion.

¶ 32 *Discovery Sanctions:* The Bank's next arguments concern the trial court's imposition of discovery sanctions. It is the Bank's position that the trial court abused its discretion when, as a discovery sanction against the Bank, it precluded Attorney Walter Weir, the Bank's former counsel from testifying. The Bank also takes a similar position with respect to the trial court's discovery sanction,

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[8] The issue of whether these allegations affected the jury's award of damages will be revisited later.

which permitted Pioneer to present to the jury evidence of the litigation conduct and discovery violations of the Bank's lawyers.[9]

¶ 33 "The decision whether to sanction a party for a discovery violation and the severity of such a sanction are matters vested in the sound discretion of the trial court. We will not reverse a trial court's order imposing such a sanction unless the trial court abused its discretion." ***Luszczynski v. Bradley,*** 729 A.2d 83, 87 (Pa. Super. 1999) (citations omitted). Under Rule 4019 of the Pennsylvania Rules of Civil Procedure, a trial court may impose sanctions for discovery violations. The factors for trial courts to consider when determining an appropriate sanction under Rule 4019 are as follows: (1) the nature and severity of the discovery violation; (2) the defaulting party's willfulness or bad faith; (3) prejudice to the opposing party; (4) the ability to cure the prejudice; and (5) the importance of the precluded evidence in light of the failure to comply. ***Id.*** at 87 (citations omitted).

¶ 34 After a thorough review of the record and of the trial court's rationale for the sanctions in light of the above factors, we cannot conclude that the trial court abused its discretion. The Bank's discovery violations were willful, repeated and persistent. The violations included the withholding of critical documents, failure to comply with requests for documents despite the entry of numerous discovery orders, production of critical documents on the eve of trial and in the middle of trial, etc. As a result of

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[9] The evidence of the litigation conduct and discovery violations was also permitted for another purpose: to show outrageous conduct (for the award of punitive damages) by the Bank.

these violations, Pioneer suffered prejudice, including, but not limited to, financial costs. The trial court's sanction – allowing the jury to hear evidence of the discovery violations – appears novel.[10] However, it is not the most severe sanction: the most severe sanction would have been the entry of a default judgment against the Bank. We express no opinion as to the appropriateness of a default judgment given the nature and magnitude of the Bank's violations. The sanction imposed by the trial court was proper under the circumstances, and we find no abuse of discretion.

¶ 35 Our review of another discovery sanction imposed by the trial court – the preclusion of the testimony of Attorney Weir during the Bank's case-in-chief – shows that the trial court did not abuse its discretion. Attorney Weir as an agent for the Bank, was part and parcel of the discovery violations at issue in this case. Therefore, the preclusion of his testimony for discovery violations is an appropriate sanction. Besides, the severity of the preclusion of Attorney Weir's testimony is tempered by the fact that Attorney Weir testified as on cross-examination during Pioneer's case-in-chief. The Bank also elicited testimony from Attorney Weir following Pioneer's cross-examination. In essence, the trial court did not completely preclude Attorney Weir's testimony. ***See*** Trial Court Opinion, 12/4/2000, at 18 n.6. Viewed in light of the five factors delineated in ***Luszczynski, supra,*** we cannot

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[10] Under certain circumstances, Pennsylvania courts have permitted jury instructions regarding a party's discovery violations such as the destruction and withholding of documents. This is the so-called adverse inference instruction. ***See*** Pennsylvania Suggested Standard Jury Instructions (Civil) 5.06; ***McHugh v. McHugh,*** 40 A. 410, 411 (1898); ***Paves v. Corson,*** 765 A.2d 1128 (Pa. Super. 2000).

conclude that the trial court abused its discretion in partially precluding Attorney Weir's testimony.

¶ 36 *The Conduct of Pioneer's Trial Counsel:* The Bank contends in its next argument that the trial court improperly permitted Pioneer's trial counsel to inflame the jury and to appeal to the jury's passion and prejudice. The Bank cites to an instance when Pioneer's counsel asked a witness if his testimony was motivated by the possibility that the jury would return a verdict in the hundreds of millions. R.R. 2704a. The above question was improper, and the trial court gave prompt curative instructions (R2704a-2705a; 2708a-2717a). However, we find that these instructions did not adequately remedy the situation. ***See Siegal v. Stefanyszyn,*** 718 A.2d 1274, 1277 (Pa. Super. 1998). It is not a stretch to conclude that this reference to a verdict in the hundreds of millions played a part in jury's subsequent award of $337 million in punitive damages.

¶ 37 The Bank also points to several instances of inflammatory language used by Pioneer's counsel during closing arguments. We agree with the Bank that counsel's improper inflammatory remarks played a significant role in the jury's award of punitive damages. We will discuss this issue further in our review of the award of punitive damages.

Damages:

¶ 38 *Consequential damages:* On the issue of consequential damages,[11] the Bank argues that the award should be

[11] Consequential damages are "losses that do not flow directly and immediately from an injurious act, but that result indirectly from the act." Black's Law Dictionary (7th Ed.) at 394.

vacated because "(i) consequential damages are not available for a claim of wrongful setoff against a bank; (ii) Pioneer did not meet its burden of proving that the alleged conversion caused its demise; (iii) Pioneer failed to make any effort to mitigate its damages; and (iv) the amount of consequential damages is unsustainable as a matter of law." Bank's Brief, at 47.

¶ 39 The Bank's argument that consequential damages are not available for a claim of wrongful setoff against a bank is without merit. The jury found the Bank liable for the tort of conversion and the consequential damages were awarded as a result of the Bank's liability for conversion. Pennsylvania law is clear that the measure of damages for conversion is the market value of the converted property at the time and place of conversion. ***Bank of Landisburg v. Burruss,*** 524 A.2d 896, 902 (Pa. Super. 1987). Pennsylvania law also provides that in tort actions in which business losses and/or lost profits are alleged to have indirectly resulted from the misconduct, consequential damages are recoverable. ***See Delahanty v. First Pennsylvania Bank, N.A.,*** 464 A.2d 1243 (1983). In the case at bar, the jury determined, based on ample evidence, that the business losses suffered by Pioneer resulted from the Bank's conversion of the Fund. Therefore, we hold that the award of consequential damages was proper.

¶ 40 The Bank's argument that Pioneer failed to prove that the alleged conversion caused its demise is meritless. Pioneer presented evidence at trial that as a result of the Bank's seizure of the Fund, Pioneer was unable to obtain a $200 million line of credit from Nikko Financial Services; that RNG was forced out of business and $4.5 million of additional RNG loans became stale. Also, as a result of the Bank's seizure of the Fund, Bank One cut off its line of

credit to Pioneer and Pioneer was unable to obtain an alternative source of credit. The above evidence amply supports Pioneer's claim, and the jury's determination that Pioneer was entitled to consequential damages.

¶ 41 The evidence also showed that Pioneer attempted to mitigate its losses. As Pioneer correctly points out, Boaz Harel testified that Leedan Business Enterprise, Pioneer's principal shareholder, invested several million dollars in an effort to keep Pioneer afloat after the Bank's seizure of the Fund. Pioneer's Brief, at 41.

¶ 42 *The measure of damages:* The Bank maintains that the measure of consequential damages was unduly speculative. Boaz Harel testified that the drop in Pioneer's market capitalization from November 26, 1997 to the date of his trial testimony was $13.6 million. This evidence was ostensibly the basis of the jury's award of $13.5 million. The Bank now argues that because market capitalization is not an appropriate or reliable measure of the value of a closely-held, thinly-traded company and because Pioneer did not establish that the decline in market capitalization was wholly attributable to the Bank's seizure of the Fund, the amount of the consequential damages was speculative. We agree with the Bank that in some instances, market capitalization alone cannot be used to determine the value of a corporation. In the instant case, as the Bank noted, the trial testimony showed that Pioneer's stock was traded over the counter and that one investor owned a controlling share of its securities. As such, the stock prices wildly fluctuated periodically. Although the stock price of a thinly traded company may be helpful in determining the company's value, it should not be the only factor in that determination. Other factors such as (1) net asset value; (2) actual market value; and (3) investment value should

also be considered. ***See In re Glosser Bros., Inc.,*** 555 A.2d 129, 133 (Pa. Super. 1989). In ***In re Glosser Bros,*** our Court also noted that in dealing with "closely-held family corporations having unlisted stocks and therefore, no public market, shares are sold too infrequently for market value to play any part in these proceedings." ***Id.*** at 135, citing ***O'Connor Appeal,*** 304 A.2d 694 (Pa. 1973). Our decision in ***In re Glosser Bros*** recognized that while the market value is to be totally disregarded only in very limited circumstances, other factors and methods of valuation should be considered as well.

¶ 43 Despite our agreement with the Bank's general statement regarding the use of market capitalization as a valuation method, our review of the record shows that during the damages phase of the trial, the Bank did indeed present alternative methods of valuation which were ultimately rejected by the jury. The Bank also presented the testimony of an expert witness who opined that the Bank's seizure of the Fund did not have a significant impact on the ability of Pioneer to operate beyond 1998. R.R. 2758a. Thus, we are not presented with a situation where the Bank was precluded from presenting alternative methods of valuation. The Bank's valuation methods and expert opinion were simply rejected by the jury while the valuation method presented by Pioneer (market capitalization) was accepted by the jury. Similarly, the Bank's argument that the drop in Pioneer's capitalization was not wholly attributable to the Bank was considered and rejected by the jury. As such, we find no reason to overturn the jury's award of consequential damages.

¶ 44 *Punitive Damages.* Throughout its brief, the Bank repeatedly maintains that Pioneer's counsel was permitted to make inflammatory arguments and allegations that

ultimately resulted in a verdict based on passion and prejudice.[12] We agree with the Bank only with respect to

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[12] Counsel for Pioneer in his closing arguments suggested that the Bank committed crimes, repeatedly called the Bank's witnesses "liars," compared the Bank to a "thug" and a "gangster" that would "knowingly steal to allow a customer to engage in kiting, to milk it for fees, and then the last second . . . shut it down and just say I'm going to take anybody's money I can." R.R. 2328a-2329a.

In addition, Pioneer's counsel baited the jury by implying that CoreStates was a Goliath and Pioneer a philanthropic David, asking: "How could you not care about the people at RNG? How could you not care at all about all of those families?" and stating without foundation: "[W]e had the government loans, the first time home buyers, the veterans. Those are the people that we lent our money to. They don't have one shred of remorse, one bit of humanity about just how many lives got turned upside down." R. 2849a. Counsel claimed that one witness had fabricated his testimony because by the time of trial he had been hired by First Union (R. 2833a) and that C.B. Cook and Walter Weir were not "people dealing with integrity" and "were caught conspiring and stealing money." For other examples, *see* R. 2837a-2838a, R. 2298a ("this deal that was working until CoreStates came in and decided to steal money"), R. 2300a ("corrupt practice, practices in racketeering, mail fraud, bank fraud, a whole host of both civil and criminal acts which they were allowing and milking for fees. We'll get to the fees that Mr. Weir milked it for as well"), R. 2308a ("the seven court orders I got * * * [are] part of the let's stone wall them to death, let's hide what we've been doing * * * because what they did is despicable. What they did is unethical. It was outrageous. And, they were hiding among every front they could. And, they got a lot to hide about"), R. 2322a-2323a ("They put on Walter Weir. How many lies did we catch him in? * * * Those are boldface lies, and he knows it. But then again, they're running for cover"), R. 2326a ("There is no limit to how despicable and outrageous their behavior is. They'll go to any lengths, because what they did in allowing this kite, in milking it for fees, both the bank and then the lawyer"), R. 2329a ("What they did was vicious, and they knew it. And to cover it up and to lie about it, and to behave the way they have, I don't know if it's criminal, but I know it's outrageous"), R. 2337a-2338a ("They let a check kiting scheme go on at CoreStates for all of 1997"), R. 2341a ("think about why it's so despicable, that not only did a bank do something that it knew was a violation of federal law and permit its customer to engage in conduct which it calls criminal, but

(Continued on following page)

the jury's award of punitive damages. Judicial reduction of a jury award is appropriate only when the award is plainly excessive and exorbitant, when it shocks the sense of justice as to suggest that the jury was influenced by partiality, prejudice, mistake, or corruption. ***Haines v. Raven Arms,*** 640 A.2d 367, 369 (Pa. 1994). A jury is given wide latitude to fashion a verdict on damages. ***Neison v. Hines,*** 653 A.2d 634 (Pa. 1995). The large size of a verdict by itself is not evidence of excessiveness. ***Layman v. Doernte,*** 175 A.2d 530 (Pa. 1961).

> The standard under which punitive damages are measured in Pennsylvania requires analysis of the following factors: (1) the character of the act; (2) the nature and extent of the harm; and (3) the wealth of the defendant. ***Kirkbride v. Lisbon Contractors, Inc.***, 521 Pa. 97, 102, 555 A.2d 800, 803 (1989) (citing Restatement (Second) of Torts § 908(2)). ***Accord Tunis Brothers Co., Inc. v. Ford Motor Co.,*** 952 F.2d 715, 740-41 (3d Cir.1991), cert. denied, 505 U.S. 1221, 112 S.Ct. 3034, 120 L.Ed.2d 903 (1992) (applying Pennsylvania law). It is for the jury to weigh these

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when it steals Pioneer's money to get it back"), R. 2834a (reference to witness: "The guy was lying * * * He was lying to protect his new employer, because they know they've got live risk"), R. 2835a ("Their own customer, the crook who had every reason in the world to say it's my money because it's going to pay down his debt"), R. 2842a ("it's more of this approach that they have to litigation and drag it all out and trial by ambush"), R. 2848a-2849a ("this is a vicious greed machine, drag it out as long as they possibly can. No heart"), R. 2852a ("what they did was diabolical . . . that kind of vicious little agenda"), R. 2858a ("When does a bank steal? Steal. That's what they did. That's what conversion is"), R. 2867a-2868a ("as I've told you: They don't have personal integrity").

Bank's Brief, at 45 n. 19.

> factors in arriving at an appropriate punitive damage award. ***Kirkbride v. Lisbon Contractors, Inc., supra,*** 521 Pa. 97, 555 A.2d 800. The excessiveness of punitive damages in a case in which they are allowable may be grounds for reversal, for a new trial, or for a remittitur under the usual rules by which the courts control the jury's award of compensatory damages. ***See*** Restatement of Torts (Second) § 908, comment d (function of jury). However, a trial judge may not declare a punitive damages verdict to be excessive simply because he or she might have awarded a lesser amount. ***Sulecki v. Southeast National Bank,*** 358 Pa.Super. 132, 138, 516 A.2d 1217, 1220 (1986) (en banc).

Sprague v. Walter, 656 A.2d 890 (Pa. Super. 1995). An appellate court can, upon proper basis and reason find that the trial court has abused its discretion in either upholding or remitting damages. ***Id.*** 929-930. According to the United States Supreme Court, judicial review of the size of punitive damage awards provides a safeguard against excessive verdicts. ***Honda Motor Co., Ltd. v. Oberg,*** 114 S.Ct. 2331, 2335, 129 L.Ed.2d 336, 343 (1994). In ***Honda,*** the Supreme Court explicitly declined to adopt or identify any particular standard of review which provides the level of scrutiny demanded by the Fourteenth Amendment. ***Id.***, at 114 S.Ct. at 2341 n. 10, 129 L.Ed.2d at 350 n. 10. However, the Supreme Court indicated that the award cannot be the result of "passion and prejudice;" the awards should not be "grossly excessive;" or "against the weight of the evidence." ***See Jackson v. Virginia,*** 443 U.S. 307, 324, 99 S.Ct. 2781, 2791, 61 L.Ed.2d 560, 576-77 (1979). In the case at bar, the improper remarks, allegations and innuendo by Pioneer's counsel warranted the grant of a new trial on the issue of punitive damages. The

jury's punitive damage award was the result of passion and prejudice. The trial court even realized, albeit in hindsight, that these inflammatory allegations and accusations by Pioneer's counsel necessarily influenced the jury's award of an astronomical $337 million in punitive damages in a case involving a dispute of about $1.8 million. Consequently, the trial court granted the bank's request for a remittitur, reducing the punitive damages award to $40.5 million. However, we find that this remitted amount still bears no reasonable relationship to the wrongful conduct.[13] Counsel cannot make arguments prejudicial to the opposing party which are not supported by facts in evidence, or which are inflammatory or beyond the limits of fair or sound argument, unduly influencing or distracting the jury. ***See, e.g., Girard Trust Corn Exchange Bank v. Philadelphia Transp. Co.,*** 410 Pa. 530, 190 A.2d 293 (1963); ***Piwoz v. Iannacone,*** 406 Pa. 588, 178 A.2d 707 (1962); ***Millen v. Miller,*** 224 Pa. Super. 569, 308 A.2d 115 (1973).

¶ 45 The Bank has carefully listed the instances in which Pioneer's counsel made allegations of criminal conduct, alleged cover-up, and made other inflammatory statements. ***See*** footnote 10. We find these instances too numerous to be harmless and we find these allegations to be unduly prejudicial. Further, we find that the trial court's grant of a remittitur in the amount of $40.5 million did not adequately remedy the harm caused. Accordingly, we will vacate the award of punitive damages and remand this matter for a new trial on the issue of punitive damages

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[13] An appellate court can, upon proper basis and reason find that the trial court has abused its discretion in either upholding or remitting damages. ***Sprague v. Walter,*** 656 A.2d 890, 929-930 (Pa. Super. 1995).

alone. We recognize that it is the province of the jury to assess punitive damages. However, the award of damages cannot be the result of caprice, prejudice, partiality, corruption or some other improper influence. ***See Gradel v. Inouye,*** 491 Pa. 534, 421 A.2d 674 (1980).

Due Process:

¶ 46 Another basis for our decision to vacate the award of punitive damages is the Due Process Clause of the Fourteenth Amendment. A decision to punish a tortfeasor by exacting punitive damages is an exercise of State power which must comply with the Due Process Clause of the Fourteenth Amendment. ***Honda,*** 114 S.Ct. at 2335, 129 L.Ed.2d at 342-43. Because punitive damages pose an acute danger of arbitrary deprivation of property, due process requires judicial review of the size of punitive damage awards. ***Id.***, 114 S.Ct. at 2340-41, 129 L.Ed.2d at 349-50.

¶ 47 The Due Process Clause of the Fourteenth Amendment protects a tortfeasor from the imposition of a "grossly excessive" punitive damages award. ***BMW of North America Inc. v. Gore,*** 517 U.S. 559, 560-61, 116 S.Ct. 1589, 1592, 134 L.Ed.2d 809, 818 (1996). The size of a punitive damages award must be reasonably related to the State's interest in punishing and deterring the particular behavior of the defendant and not the product of arbitrariness or unfettered discretion. ***Id.*** at 567-68, 116 S.Ct. at 1595, 134 L.Ed.2d at 822. Under the U.S. Supreme Court jurisprudence, the following must guide a court's review of the propriety of a punitive damages award: the degree of reprehensibility of the defendant's conduct, the ratio of punitive damages to the actual or potential harm inherent

in that conduct, and the existing civil and criminal penalties for similar conduct. ***Id.*** at 573-82, 116 S.Ct. at 1598-1603, 134 L.Ed.2d at 826-33.

¶ 48 The degree of reprehensibility is the primary indicator of the reasonableness of a punitive damages award. ***Id.*** at 575-77, 116 S.Ct. at 1599, 134 L.Ed.2d at 826. The reprehensibility inquiry takes into consideration the fact that some wrongs are more blameworthy than others. ***Id. See Shiner v. Moriarty,*** 706 A.2d 1228, 1241 (Pa. Super. 1998). With regard to the Bank's argument regarding the proportionality of the punitive damages to the compensatory damages, we note that under Pennsylvania law, punitive damages need bear no proportional relationship to the compensatory damages awarded in a particular case. Rather, a reasonable relationship must exist between the amount of the punitive damage award and the twin goals of punishment and deterrence, the character of the tortuous act, the nature and extent of the harm suffered by the plaintiff, and the wealth of the defendant. Mathematical proportionality is not required between punitive and compensatory damages. Although there are no mathematical formulae or hard and fast rules about the relationship between the tortuous conduct and the amount of punitive damages, our review of the record shows that the punitive damage award of $337 million (remitted to $40.5 million) bears no reasonable relationship to the Bank's conversion of the Fund. The unreasonableness and gross excessiveness of the jury's award is buttressed by the fact that $337 million is the highest punitive damage award in Pennsylvania history. It is inconceivable that the Bank's conduct in this case was the most reprehensible and the most blameworthy conduct in Pennsylvania history. Furthermore, we reiterate that the

remittitur of $40.5 million is still excessive and does not bear any reasonable relationship to the Bank's wrongful conduct. Therefore, this unreasonable punitive damage award cannot stand. Due to our resolution of the punitive damages issue, we need not address other aspects of the Bank's argument on this issue.

¶ 49 In conclusion, based on the foregoing discussion, we find that the amount of punitive damages in this case is grossly excessive and shocks our sense of justice. ***See Lewis v. Pruitt,*** 487 A.2d 16, 22 (Pa. Super. 1985) (this Court will not find a verdict excessive unless it is so grossly excessive as to shock our sense of justice). Based on the foregoing discussion, we affirm the judgment of the trial court with respect to liability, compensatory damages, and consequential damages. We vacate the award of punitive damages in the amount of $40.5 million, and remand for a new trial solely on the issue of punitive damages.

¶ 50 Affirmed in part and reversed in part. Remanded for a new trial with respect to punitive damages. Jurisdiction relinquished.

¶ 51 BECK, J. files Dissenting Opinion.

DISSENTING OPINION BY BECK, J.

¶ 1 I respectfully dissent from the majority's decision to affirm the judgment with regard to liability for conversion. I believe the common law cause of action of conversion is inapplicable. This case is controlled by Article 4A of the Uniform Commercial Code, which governs the procedures, rights, and liabilities arising out of commercial electronic

funds transfers. The AFMC Funds Transfers at issue were clearly governed by Article 4A, which authorized CoreStates's conduct in accepting and setting off the Funds Transfer. Contrary to the majority's conclusion, I believe that CoreStates acted within its rights under Article 4A-502 because I agree with CoreStates that ultimate ownership of the funds is not relevant under Article 4A. Moreover, common law principles of ownership that vary from state to state are ill-suited for the national regulation of financial institutions.

¶ 2 The position that the U.C.C. controls this case is supported by the Official Comment to Section 4A-102 which states that

> [b]efore this Article was drafted there was no comprehensive body of law – statutory or judicial – that defined the judicial nature of a funds transfer or the rights and obligations flowing from payment orders. Judicial authority with respect to funds transfers is sparse, undeveloped and not uniform. Judges have had to resolve disputes by referring to general principles of common law or equity . . . but attempts to define rights and obligations in funds transfers by general principles or by analogy to rights and obligations in negotiable instrument law or the law of check collection have not been satisfactory . . . The rules that emerge represent a careful and delicate balancing of interests and are intended to be the exclusive means of determining the rights, duties, and liabilities of the affected parties in any situation covered by particular provisions of the Article. Consequently, resort to principles of law or equity outside of Article 4A is not appropriate to create rights, duties and

> liabilities inconsistent with those stated in the Article.

U.C.C. § 4A-102, Official Comment.

¶ 3 Furthermore, many courts have found that common law claims, such as conversion, are precluded when such claims would impose liability inconsistent with the rights and liabilities expressly created by Article 4A. ***See, e.g. Grain Traders, Inc. v. Citibank,*** 160 F.3d 97 (2d Cir. 1998) (finding that plaintiff's claim for conversion was precluded under state's commercial code as inconsistent with commercial code); ***Banco de la Provincia de Buenos Aires v. BayBank Boston N.A.,*** 985 F.Supp. 364 (S.D.N.Y. 1997) (stating that for conversion claim to stand it cannot be inconsistent with Article 4A); ***Cumis Ins. Soc., Inc. v. Citibank, N.A.,*** (921 F.Supp. 1100) (S.D.N.Y. 1996) (finding claim for conversion failed because bank's actions were expressly authorized by Article 4A).

¶ 4 There are sound policy reasons underlying the conclusion that Article 4A pre-empts inconsistent provisions of state law. Having a uniform method of transferring funds provides a national set of rules and regulations giving the system discipline, stability, predictability, efficiency, liquidity and finality. The integrity of this complex system will be compromised if state actions inconsistent with Article 4A are permitted against participating institutions. If the U.C.C. has established an imperfect vehicle for the transfer of funds then the proper course is to amend the U.C.C. rather than impair the effectiveness of the system by injecting inconsistent common law tort actions.

Court of Common Pleas of Pennsylvania,
Philadelphia County.
Pioneer Commercial Funding Corp.
v.
American Financial Mortgage Corp.
No. 0885.

April Term, 1998.
December 4, 2000.

Maurice R. Mitts, for plaintiff.

David R. Moffitt, for defendants American Financial Mortgage Corp. and Flatley.

Michael M. Baylson, Nolan N. Atkinson Jr., Hon. *Arlin M. Adams* and *Ralph G. Wellington*, for defendant First Union/CoreStates.

COHEN, J.

The court has before it the post-verdict motions of defendant CoreStates Bank NA., as well as post-verdict motions of defendants American Financial Mortgage Corporation, Thomas F. Flatley, and plaintiff Pioneer Commercial Funding Corporation which were filed in the aftermath of a long, bitterly contested trial. Testimony in this matter began on June 2, 2000. The jury returned a verdict on July 26, 2000. The jury awarded the plaintiff, Pioneer Commercial Funding Corporation, $13.5 million in consequential damages and $337.5 million in punitive damages against the bank. This was a bifurcated trial. After the liability phase, concluding June 30, 2000, the jury found that defendants CoreStates and American Financial Mortgage Corporation were liable in conversion to the plaintiff, Pioneer, in the amount of $1,779,519.99. The court directed a verdict on a contract claim against

defendants American Financial Mortage [sic] Corporation and Thomas Flatley.

After reviewing the post-verdict motions filed by all defendants, reviewing their briefs and memoranda, and after hearing argument, this court by means of the within appropriate orders will deny judgment n.o.v. in favor of AFMC on the conversion claim, deny judgment n.o.v in favor of both AFMC and Flatley on the contract claim, affirm the jury's award against CoreStates as it pertains to its liability in conversion and consequential damages, and, furthermore, grant CoreStates' motion for remittitur. Pursuant to the remittitur, the court will set punitive damages at $40,500,000, which amount plaintiff is to accept or, in the absence of its acceptance, be subject to a new trial on the sole issue of punitive damages.

The court hereby denies the post-verdict motions of defendants on every other ground cited. Finally, the court will grant Pioneer's request to recover attorneys' fees, costs and interest at the contract rate from AFMC and Flatley and the plaintiff's request to recover prejudgment interest from CoreStates Bank. Plaintiff's request to otherwise mold the verdict is denied.

FACTUAL BACKGROUND

The plaintiff in this matter alleged, and the jury agreed, that until the late fall of 1997 it was a thriving mortgage funding company with a bright future. In November 1997, however, Pioneer innocently fell victim to the unfounded assertion of CoreStates Bank of its common-law right of setoff. Unbeknownst to Pioneer, its partner in a loan and security agreement, AFMC, through its principal, Thomas Flatley, was caused to be overdrawn

in checking accounts it maintained at CoreStates in excess of $4 million with the tacit complicity of the bank. On November 6, 1997, upon discovery of its loss due to the "check kiting" scheme, CoreStates imposed a debit restraint on all the accounts of AFMC and its affiliates. On November 25, 1997, AFMC, through its lawyer, notified the bank and provided proof that an affiliate in a mortage [sic] loan transaction, Norwest, had wrongly and mistakenly deposited into AFMC's settlement account at CoreStates some $1.7 million.[1]

Despite this notification, CoreStates, in a desperate attempt to recoup its negligently incurred losses, seized the funds pursuant to its alleged right of setoff. Instead of contesting the seizure, AFMC and Thomas Flatley entered into a workout agreement with the bank whereby the parties conspired to keep Pioneer's money and to keep the matter secret. The resulting effect was the severe impairment of capital and business credibility of plaintiff. It ceased operations and went out of business.

To quote directly from the capable brief filed with this court by CoreStates, "There is no dispute that AFMC owed money to both Pioneer and CoreStates." (*See* brief of defendant CoreStates at p. 3.) That is the watershed question. In the view of Pioneer, supported by this jury's verdict, Pioneer enjoyed the exclusive right of ownership

[1] This is the way the transaction broke down: On November 12, 1997, Norwest wired $1,454,699.80 into AFMC's account; on November 13 Norwest wired $209,984.33, and on November 19, 1997, Norwest wired $114,835.86 into the CoreStates account owned by AFMC. (*See* N.T. 6/6/00 a.m. pp. 45-56; 6/15/00 a.m. pp. 33-36; and supporting exhibits T-723 and T-5005.) Thus, the total amount wired into AFMC's account at CoreStates was $1,779,519.99.

in the sums that Norwest mistakenly wired into AFMC's account. It is the contention of CoreStates that the long and respected common-law right of setoff vested in CoreStates' ownership rights to any amounts of money it found in any account of AFMC's at any time after the imposition of the November 6 debit restraint.

The court first addresses the contentions of defendant CoreStates, followed by those of defendants AFMC and Flatley and plaintiff Pioneer.

I. Judgment n.o.v.-Legal Issues

(A) Whose Money Was It, Anyway?

In order to determine who owned the funds at issue the court believes that the determinative testimony was that of Melanie Holtz, senior vice president of RNG; Glenda Klein of Pioneer; Howard Seidman, executive vice president of AFMC; and Joseph Scheuren, vice president of AFMC. Collectively, the four testified that Norwest committed to purchase two portfolios. Exhibits T-138 and T-146 evidence the first portfolio and T-143 and T-147 evidence the second portfolio. It was Melanie Holtz and Glenda Klein who discovered that Norwest mistakenly wired payment for the first portfolio to AFMC's settlement account at CoreStates. It is critical to understanding the history of this transaction to note that Norwest's first mistake was reversed within hours and the money representing the first portfolio was deposited in Pioneer's account at Banc One, as it should have been.

After the experience of the first group of loans, Holtz, Klein and Seidman all contacted Norwest to insure that a second mistaken deposit would not occur. Holtz sent Norwest specific instructions directing it how to wire the

money. These instructions were signed by Howard Seidman. (*See* N.T. 6/12/00 p.m. pp. 94-96.) Moreover, Holtz called a Dana Gibbs at Norwest to further ensure that Ms. Gibbs received the wiring instructions. Ms. Gibbs assured Ms. Holtz that Norwest would honor the instructions. (*Id.* at 96.) According to Melanie Holtz, she took these special precautions "as soon as I found out the first wire did not go to Banc One." (*Id.* at 97.)

CoreStates strenuously argues that Pioneer was mistaken in its contention that AFMC never owned the monies that were taken by means of setoff because AFMC never acquired any interest in the loan packages of RNG, a loan originator, which has filed in bankruptcy. In support of this argument, CoreStates underscores that the loans endorsed to AFMC were without conditions and in turn endorsed by AFMC to Norwest "unconditionally" without identifying Pioneer's security interest. CoreStates further cites the parol evidence rule for the proposition that the documents at issue must speak for themselves and the actions of the parties surrounding the transactions have no effect on the ultimate factual determination of who owned the contested funds.

Pioneer did, indeed, own the notes as the jury so held. This was certainly the understanding of the parties as emphasized by the testimony of Howard Seidman. (N.T. 6/13/00 p.m. pp. 45-51; 85-91.) Testimony by Glenda Klein and Melanie Holtz also illuminates the nature of the transaction at issue.

1. The significance of the parol evidence rule

The Supreme Court of Pennsylvania defines the parol evidence rule as follows:

"Where the alleged prior or contemporaneous oral representations or agreements concern a subject which is specifically dealt with within the written contract, and the written contract covers or purports to cover the entire agreement of the parties, the law is now clearly and well settled that in the absence of fraud, accident or mistake, the alleged oral representations or agreements are merged in or superseded by the subsequent written contract, and parol evidence to vary, modify or supersede the written contract is inadmissible in evidence."

This court specifically holds that the parol evidence rule is inapplicable to the sale of loans under review. The parol evidence rule enters the picture when the central player in the contractual drama is a completely integrated agreement. It is abundantly clear that no single agreement governs the relationships among the parties in this setting. *See McGuire v. Schneider Inc.*, 368 Pa. Super. 344, 349-50, 534 A.2d 115, 118 (1987).

2. Other indicia of ownership

The record in this case is heavy with testimonial and demonstrative evidence tending to show by a strong preponderance that Pioneer owned the notes and the proceeds involved in the AFMC/Norwest/RNG transactions. In addition to the testimony already cited, the jury saw the bailee letter attached to the notes. These letters express the ownership, interest of Pioneer and Banc One in the notes and proceeds, which the court, and obviously the jury, believed to be clear and irrefutable proof of ownership of the funds. Furthermore, on November 25, 1997, AFMC's attorney, David Moffitt, a lawyer in a greatly respected firm, wrote a letter to CoreStates requesting

that it return the funds so that they may be sent "to the intended recipient of the wires, Pioneer Bank." (emphasis supplied) The jury saw this letter at T-1000 and could not ignore it. The jury's finding that the loan proceeds were the property of Pioneer is supported by the evidence. CoreStates' motion for post-verdict relief on this issue, i.e., ownership of the loan proceeds, is denied.

(B) The Significance of Regulation J

CoreStates further maintains that because the funds at issue were directed to the settlement account of AFMC at CoreStates by means of a federal wire transfer, the plaintiff's claims are controlled by article 4(a) of the Uniform Commercial Code, 13 Pa.C.S. § 4(a)101 et seq. and Federal Reserve Board regulation J, 12 C.F.R. part 210. Citing the foregoing provisions, CoreStates argues that its setoff of Pioneer's money from AFMC's settlement account to satisfy AFMC's overdrafts could not constitute conversion because such a setoff was specifically authorized under the applicable provisions of the UCC. In support of its argument, CoreStates most strenuously cites two federal district court cases (which are not and never have been binding on this court), viz *Community Bank F.S.B. v. Stephens Financial Corporation*, 966 F. Supp. 775 (N.D.Ind. 1997) and *Cumis Ins. Soc'y Inc. v Citibank N.A.*, 921 F. Supp. 1100, 1109-10 (S.D.N.Y. 1996). Both cases seem to hold that regulation J, in that it is federal law, pre-empts the common-law claim of conversion, which is the plaintiff's theory of recovery in this case. However, this court finds that the cited cases do not and never did apply to the scenario that was before the jury. While the factual situation in *Community Bank* may be somewhat similar to the set of facts at hand, there are obvious

differences which mandate the opposite result. In *Community Bank*, a debtor owed money to a finance company. The finance company told the debtor to wire the funds it was owed to its warehouse lender, Chase Manhattan Bank. Instead, the debtor wired the funds to another bank, to which the debtor's creditor owed money. Hence, the other bank set off the amount that it was owed before returning the excess to the debtor. In the meantime, the debtor had paid another amount of money to the correct bank. Hence, the debtor wanted its money that was wrongfully deposited and setoff returned.

In *Community Bank*, the court did indeed hold that article 4(a) of the Uniform Commercial Code as the Pennsylvania statutory embodiment of regulation J pre-empted the common-law action by the debtor but only after addressing four questions that seem to open up the common-law action: (1) was the wire transfer an authorized payment as defined by the UCC; (2) which party owned the funds at the time of setoff; (3) was the debtor's attempt to cancel binding on the bank that performed the setoff; and (4) was the setoff appropriate under the applicable law? *See Community Bank*, 966 F. Supp. at 781.

In citing *Community Bank*, the defendant attempts to compare the orange of that case with the apple of the facts under the current case. This court has already explained that the ownership interest on the part of Pioneer had been fully established by the time CoreStates exercised its setoff-December 18, 1997.

Looking also at the *Cumis* case, the court finds that the defendants are attempting to fit a different set of facts into the instant framework. In *Cumis*, an imposter caused the fraudulent wiring of money from an account at

Benchmark in West Chester, Pennsylvania, to an account at Citibank in New York. The same imposter, 13 days later, deposited a forged treasury check into the account of Mario Adler at Benchmark. Four days after that deposit, the imposter called Benchmark seeking to transfer more money to the Citibank account. Benchmark tried to get the wrongly deposited money back in a series of wires it sent via CoreStates. Meanwhile, the holder of the account at Citibank had withdrawn the money necessary to cover the fraudulent transfers. The plaintiff was Benchmark's insurer. After paying Benchmark the amount of money it lost, the plaintiff insurer sued Citibank. The plaintiff alleged fraud because an agent of Citibank had told CoreStates when it tried to reclaim the money that the money previously transferred had been withdrawn and that was not so. Or, as the court put it, Citibank's representative told Benchmark (CoreStates) "There was nothing [it] could do to recover the money-essentially, don't bother, the money's gone." 921 F. Supp. at 1103. The court upheld the plaintiff's argument that the allegedly false statement could be the basis of fraud. *Id.*

The court in *Cumis* then delves into the question whether Benchmark relies on Citibank's erroneous statement in refraining from resending a telex requesting the return of wire transfers as a "tested telex with an indemnification" causing it to forego other means by which it could have secured the return of the funds. Citibank replied that it had no obligation to return the wire transfer funds to Benchmark.

In *Cumis*, the effect of article 4(a) of the UCC is to characterize Citibank as a receiving bank which had an obligation to pay funds over to a beneficiary. It could have returned the funds or not returned the funds at its

discretion. However, as the court points out, the commentary to the UCC section does not relieve the bank from liability. *See* 921 F. Supp. at 1105. The defendant relies on *Cumis* for the proposition that in circumstances such as those that were before the jury in this case, UCC article 4(a) has a wide and exclusive reach. However, the facts in *Cumis* differ immensely from the facts in the current case. In *Cumis*, the plaintiff could not allege that there was any agreement to return the funds. *See* 921 F. Supp. at 1110. In the current matter, there was an understanding among the parties that the funds did not belong to AFMC. There was sufficient communication among the parties for defendant to know – and the jury so held – that the money at issue belonged to Pioneer.[2]

The defendants' motion for a new trial and/or judgment n.o.v. on the foregoing ground is therefore denied.

(C) Significance of the Bankruptcy

The defendant argues that because RNG was in bankruptcy at the time Pioneer funded the mortgage loans at issue, and although the loan and security agreement between RNG and Pioneer predated the bankruptcy and granted a continuing lien and security interest to Pioneer in all of RNG's existing and after-acquired mortgage loans, the United States Bankruptcy Code at § 552 "cut off the effect of that security agreement." (*See* brief of defendant

[2] The court notes with interest that the defendant refrained from addressing the tangled facts in the *Cumis* case in its brief. However, the court holds the defendant blameless because, other than setting forth a circumstance in which the UCC provision applies, the *Cumis* case features a widely disparate set of facts and does not squarely deal with a setoff.

at p. 4.) Accordingly, the defendant argues that without bankruptcy court approval of the security interest, Pioneer can assert no property interest in the loan proceeds.

The court finds the Bankruptcy Code inapplicable. As the plaintiff points out in its brief, Pioneer took title to the notes through what the plaintiff calls "an absolute assignment" of the notes from RNG in the ordinary course of business. The court further holds that there was sufficient indicia, e.g. the bailee letters T-146, T-147, of ownership on Pioneer's part. The plaintiffs correctly characterize this ownership interest as a "perfected security interest" vesting rights independently in Pioneer.

Defendant's motion for post-verdict relief on the foregoing ground is therefore denied.

(D) Section 606 of the Banking Code

CoreStates argues that the jury's verdict was contrary to law because as a predicate to preventing setoff or debit restraint by the bank, section 606 of the Pennsylvania Banking Code and the Uniform Commercial Code required Pioneer to obtain a court order or post a bond.

In support of its position the bank cites *E.F. Houghton & Co. v. Doe*, 427 Pa. Super. 303, 628 A.2d 1172 (1993). In *Houghton*, an investment clerk employed by the plaintiff stole from it a million dollars in treasury notes and deposited them in two accounts at Mellon (then Girard) Bank. The dishonest employee then used these funds as collateral to obtain a $150,000 loan from the bank. The loan agreement provided that in the event of default the bank was entitled to withdraw $150,000 plus accrued interest from the account of the dishonest employee to pay the

debt. 427 Pa. Super. at 305, 628 A.2d at 1173. The thieving employee's employer discovered the theft, sued the employee and his wife and obtained a judgment against them. Before it received a writ of attachment directed to the funds, Mellon exercised its rights under the loan agreement and withdrew the stated principal and interest from the account. It is unquestionable that the account holders owed Mellon the required amount. Further, Mellon paid the thief's employer the balance.

In turning down the employer's request for the balance of the stolen money, the Superior Court follows the literal language of the Banking Code. 7 Pa.C.S. § 606. The cited section indeed requires that a party asserting an interest in funds: "(i) obtain and serve on the institution an appropriate order directed to the institution by a court restraining any action with respect to the account or property until further order of such court or instructing the institution to pay the balance of the account or deliver the property in whole or in part as provided by the order or (ii) deliver to the institution a bond in form and amount and with surety satisfactory to the institution, indemnifying the institution against any liability, loss or expense which it might incur because of its recognition of the adverse claim . . . . "

The very well-reasoned opinion of Judge Beck in *Houghton* sharply distinguishes the facts of this case from the facts therein. The court states:

> "Cases which prohibit setoff by the bank are inapplicable to the circumstances of this appeal. This appeal does not involve deposit funds held for the benefit of a third party in a trust, fiduciary or agency context." 427 Pa. Super. at 309, 628 A.2d at 1175-76 citing *Sherts v. Fulton Nat'l*

Bank, 342 Pa. 337, 21 A.2d 18 (1941) and *Ryan Brothers Inc. v. Curwensville State Bank*, 382 Pa. 248, 114 A.2d 178 (1955).

And there is no question that under the facts of the current case, as in *Sherts*, the funds that AFMC held in trust for another under a fiduciary or agency relationship were not available to the bank for payment of debts owed by the individual debtor who happened to be the account holder in this case. *See Houghton*, 427 Pa. Super. at 309-10, 628 A.2d at 1175-76.[3] Because section 606 of the Banking Code does not apply to the underlying transaction herein,

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[3] Any doubt as to whether the funds at issue in this case were held in trust should be resolved with reference to the so-called Moffitt letter, T-1000. On November 25, 1997, David Moffitt, Esquire, attorney for AFMC, wrote to CoreStates to inform them that the funds wired into the settlement belonged to Pioneer. Moffitt enclosed a copy of the bailee letter and specifically requested that the bank undo the wires. The bailee letter says:

> "The enclosed notes . . . and other documents ("collateral") . . . have been assigned and pledged to (a) Pioneer Commercial Funding Corp., ("borrower") as collateral under a loan and security agreement. . . . The collateral is being delivered to you for a purchase under the existing take out commitment. . . . Either payment in full for the collateral or the collateral itself must be received within 45 days after the date of this letter. Until the time you are deemed to be holding the collateral in trust, subject to the security interest granted first to borrower and then to agent for lenders and as agent's bailee in accordance with the applicable provisions of the Uniform Commercial Code. . . . Payment for collateral must be made by wire transfer or immediately available funds to: Banc One, Texas N.A., agent account . . . credit: Pioneer Commercial Funding Corp. . . . "

Banc One's representative, Gloria Sadler, testified that the aforesaid bailee letter accompanied the notes when they left Banc One and were shipped to AFMC. *See* N.T. 6/7/00 p.m. pp. 74, 85.

the court will deny CoreStates' petition for post-verdict relief on this ground as well.[4]

II. New Trial Issues

(E) The Court's Instruction on Liability Was Correct

Defendant CoreStates requests that this court order a new trial holding that it erred as a matter of law in instructing the jury on "liability." CoreStates states: "The court's charge was confusing." Initially, CoreStates contends that the court should have explained what the defendant considers to be the applicable provisions of the Uniform Commercial Code, Federal Banking Regulation J, the United States Bankruptcy Code and the Pennsylvania Banking Code to the jury. However, the court has held herein, and previously held as a matter of law, that these provisions do not apply to the events that gave rise to this lawsuit.

The Supreme Court of Pennsylvania held in *Stewart v. Motts*, 539 Pa. 596, 654 A.2d 535 (1995) that "Error in a charge is sufficient ground for a new trial, if the charge as a whole is inadequate or not clear or has a tendency to mislead or confuse rather than clarify a material issue."

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[4] The court further holds that section 9306 of the Pennsylvania UCC, 13 Pa.C.S. § 9306(b), is inapplicable to the current facts because of the foregoing analysis, viz that AFMC was in a fiduciary relationship to Pioneer. Further, the argument that CoreStates advances in support of the proposition that Pioneer, pursuant to the foregoing section of the UCC never had a security interest, emerged during a colloquy concerning a proposed point for charge. (*See* N.T. 6/29/00 p.m., pp. 94-98.) But the thrust of that argument was that the court was required in the defendant's view to charge the jury in the words of the UCC. This court adequately instructed the jury on the elements of a security interest by means of its charge without following the language of the UCC.

539 Pa. at 606, 654 A.2d at 540, citing *Glider v. Commonwealth, Department of Highways*, 435 Pa. 140, 151-52, 255 A.2d 542, 547 (1969). The court further held that a new trial is in order on the basis of an inadequate charge if the charge under review fails to make the issues clear to the jury or if there was a "prejudicial omission of something basic or fundamental." *Id.* In order to determine whether there was such an omission or whether the charge was misleading or in some sense prejudicial, the reviewing courts look at the charge "as a whole."

This court, upon review of its own charge, holds that no issue was omitted and that the charge as a whole adequately instructed the jury.

In addition to its repeated contention that the foregoing statutory and regulatory provisions somehow should have been incorporated into the charge-a contention that the court has repudiated-the defendant further complains that this court failed to tell the jury that its actions would have freed it of liability had the jury found that it acted in good faith. To paraphrase the Supreme court in *Stewart*, while words such as "good faith" and "high degree of care" have their champions among lawyers they have no "talismanic properties" requiring that they always be used in instructing the jury in cases of this description. The inquiry is not whether this court used the precise words that the defendant wanted it to use, but whether it adequately guided the jury in carrying out its task of weighing the facts in accordance with the law. *Id.* The court spelled out the elements of conversion, and in noting that CoreStates and AFMC had the right to rely on the advice of counsel in taking the actions that they did, placed the good

faith defense before the jury. Accordingly the defendant's request for a new trial on this ground will be denied.[5]

(F) The Fairness of the Proceedings

CoreStates demands a new trial "in the interest of justice" citing a "fundamental lack of fairness in the proceedings." In support of this claim, the defendant spells out the following grounds:

"(1) The trial was unfair because plaintiff was permitted to expand its scope on the eve of trial and CoreStates' defense was then hampered by its late need to change counsel and preclusion of the testimony of its lawyer and chief witness.

"(2) The trial was unfair because Pioneer was allowed to present an unpleaded 'conspiracy theory' under which inflammatory and inadmissible evidence was admitted against CoreStates.

"(3) The trial was unfair because erroneous trial rulings prevented CoreStates from adequately presenting its case.

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[5] Elsewhere in the defendant's brief, CoreStates takes issue with this court instruction on causation where it applies to the plaintiff's burden of proof. The defendant believes the court erred by telling the jury that the setoff had to be a "significant factor" in causing the business harm to Pioneer rather than a substantial factor. The plaintiff, however, is correct in pointing out that: (1) the courts permit significant to be used in place of substantial (*see Jeter v. Owens Corning Fiberglas Corp.*, 716 A.2d 633, 636 (Pa. Super. 1998)) and (2) the court used adjectives significant and substantial interchangeably and on the record (*see* N.T. 7/26/00 p.m. pp. 82-83).

"(4) The trial was unfair because the trial judge refused to recuse himself.

"(5) The trial was unfair because of the improper conduct of Pioneer's counsel before the jury."

The court will deal with these contentions in order of their presentation.

Preliminarily, the court must observe that trial of this matter, the outcome of which was of critical interest to all parties, turned out to be a highly contentious affair. Nonetheless, amidst the exchange of objections, barbs, and ex cathedra comments, the parties were able to present the jury with respectively clear versions of their positions. The court cannot find fault with the comprehensive state of preparation and generally professional conduct of all attorneys involved in this case.

1. Were the sides lined up unequally at the starting gate?

(a) Pretrial rulings: discovery proceedings

Buried in footnote 18 on page 18 of CoreStates' brief is the following statement: "Discovery was contentious and hindsight demonstrates that it would have been prudent for CoreStates to have handled some of those issues in another way." Indeed. As CoreStates inferentially concedes, the contentious atmosphere that pervaded trial of this case flowed from the contumacious response of CoreStates to the plaintiff's reasonable, if repeated, discovery requests. The nadir of this trial occurred on June 28, 2000, when the bank produced a parcel of probative documents it clearly had at its disposal for years. On that day, both CoreStates' prior counsel, Walter Weir, Esquire, and its

incumbent trial counsel, Michael Baylson, Esquire, abashedly acknowledged that, having waived a supposed lawyer-client privilege that they believed protected these documents back on June 5, the documents still were not produced until June 28, which was, in dramatic terms, the middle of the third act of this trial. Quoth Mr. Weir: "It didn't occur to me that those documents were sitting there and hadn't been produced until yesterday." (N.T. 6/28/00 a.m. p.10.) Quoth Mr. Baylson: "I think Mr. Weir and I were under the belief that at that time we were making a full and complete production of the privileged documents. Obviously we were not . . . . " (*Id.* at 11). Mr. Baylson generously extended himself as a helpmate to the court in this matter. He said: "Not to lessen the seriousness of this, but to mitigate its impact on the trial" that a recess would be in order to permit the plaintiff to examine the unearthed discovery. Mr. Baylson added the following gloss: "It's my opinion, having looked at them, a couple last night and this morning, that the number of substantive documents that say anything substantive are less than 20, about 20 . . . ." (*Id.* at 12.) CoreStates' counsel concluded: "I can say to your honor, I don't think there's been any bad faith or purposeful hiding here. At the most, this is an oversight." (*Id.* at 16.)

Ultimately, the court made a finding as a matter of law that "There was a misconduct on the part of the defense by failing to turn this over at the time it was supposed to have been turned over." (N.T. 6/28/00 p.m.

p. 43.) The court then precluded Mr. Weir from testifying for the defense. (*Id.*)[6]

2. Other indicia of unfairness

CoreStates further complains that this court should have recused itself from these proceedings because, in effect, as the bank alleges, the court had formed a fixed opinion of CoreStates' liability in this matter and, thus, could not be fair. CoreStates bases its argument upon the affidavit of a Robert Sayre, Esquire, an associate of the aforementioned Walter Weir. Mr. Sayre's affidavit was attached to a recusal motion the bank defendant filed prior to trial. The bank sought recusal of the court based upon rulings that did not go its way-principally, discovery matters, motions for summary judgment (in which volumes were filed while holding back discovery), and the court's hypothetical characterization which occurred during an off-the-record pretrial conference of what a jury might conclude about the conduct of the party defendants in this matter. The court did say what the defendant bank alleges it said. In an unfortunate attempt at levity the court even referred to CoreStates' successor, First Union, as "First Onion." In the latter respect, the court was behaving as Gilbert & Sullivan's "Nisi Prius nuisance, who

[6] CoreStates, in effect, characterizes the preclusion of Mr. Weir as having a devastating effect on its case. Indeed, the court's sanction was rather velvet-gloved in that Mr. Weir had already testified as of cross-examination and been directly examined comprehensively. To suggest that Mr. Weir's absence from the dramatis personae of the extensive defense presentation was a mortal blow is mystifying under the testimonial circumstances of this case.

just now is rather rife, the judicial humorist . . . . "[7] The court is now constrained to say in its own defense that based on its recall of the circumstances that prevailed in the spring of 2000, that its comments came purely as a response to the overly contentious behavior of the parties. During pretrial conferences on the motions for summary judgment, lawyers for all parties could not restrain themselves in hurling fusillades of accusations and abuse upon one another. This court was put in the position of a mediator and at times had to intervene in an attempt to steer the discussion back to the merits.

As to the hypothetical scenario that the court expressed, the court recalls the hypothesis came in the midst of a discovery argument during which the bank was strenuously urging the court to preclude T-15, the settlement agreement arrived at between AFMC and CoreStates. The court's hypothesis was aimed at testing whether the disputed document would be relevant to either party under a "worst case scenario." Thus, the court views its hypothesis as no better or no worse than any "What if . . . " question hurled at an advocate by any court in any courtroom in this land. What is more, in that the expressed hypothesis and any other comment made by the court appeared nowhere in this voluminous record nor was uttered in the presence of the jury or any neutral factfinder, the defendant has failed to prove that any comment the court might have made infected these proceedings so as to guide the ultimate outcome.

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[7] *See* "I've Got a Little List," The Mikado, A Treasury of Gilbert & Sullivan, Taylor, Deems (Ed.), 1941, p. 257, Simon & Schuster, New York.

This judge is further constrained to add that he has handled over one hundred cases involving either CoreStates Bank, First Union Bank or Walter Weir's law firm. An accusation of bias or prejudice is unworthy. New counsel, Judge Arlin Adams, in his brilliant argument to this court refused to raise the issue of recusal. Further, it is the duty and obligation of a diligent trial judge in a jury case to evaluate the positions of both sides of a dispute in order to encourage or effectuate settlement. In this case, the lawyers for the bank were in actuality defending their own conduct which led to the suit. In essence, they were representing themselves. Their oversensitivity is manifest and even possibly understandable.

3. Was it unfair to deny a continuance?

This defense contention can be dealt with very briefly.

CoreStates requested a continuance after it became clear that its counsel, Walter Weir, Esquire, would principally function as a witness in this case. After consultation with the supervising judge, this court did deny the request for the continuance. Trial counsel, Mr. Baylson, entered his appearance. The trial proceeded. No prejudice resulted because nowhere during the following two months of trial did it appear plain that Mr. Baylson or his eminent co-counsel, Nolan Atkinson, Esquire, were in any way, shape or form unprepared or lacking in skill or hobbled by the comparatively brief run up to the presentation of their case.

Furthermore, again, the defendant complains too much. Mr. Weir's presence loomed large among the facts of this case from winter of 1997 to the date of trial. Mr. Weir certainly knew, for at least two months and as long as 20

months, that his role as counsel for CoreStates and the person who made critical decisions about the setoff posed a possible conflict. For CoreStates to complain that it did not anticipate the change of counsel at this point is nothing but the injection of an empty issue into its cause. Especially in view of the highly professional, well-versed and skillful performance of its replacement counsel, no error can be ascribed to this court's denial of a continuance.

4. Whether the discovery abuses should have been heard by the jury

To support its straightforward conversion claim, the plaintiff alleged that the defendants-CoreStates Bank and AFMC-found means to cover up the alienation of Pioneer's money. As a component of this theory, the plaintiff sought to prove that the workout agreement entered into by the defendants was shaped in such a way that the act of conversion would acquire legitimacy. Accordingly, to resist proof of this theory, the defendants tried by every means possible to keep the workout agreement and all evidence associated with it out of the record. There were an unheard of seven discovery orders entered against CoreStates. Hence, there was a close correspondence between the defendant's behavior in the discovery stage of this trial and their conduct during the operative moments attendant to the conversion of Pioneer's money. It follows that Pioneer had every forensic reason to place CoreStates' erratic and resistant response to reasonable discovery requests before the jury.

CoreStates argues that this court went beyond its power to administer discovery sanctions in permitting the discovery disputes to be played out before the jury. In essence, CoreStates suggests that it would have been

sufficient for the court merely to sanction it for its admitted discovery abuses and that permitting the jury to hear discovery conduct was the ultimate sanction. In support of its argument, CoreStates cites a federal district court case from the *Northern District of Illinois, Empire Gas Corp. v. American Bakeries Co.*, 646 F. Supp. 269 (N.D. Ill. 1986) holding that exclusion of evidence of pretrial discovery disputes is proper under federal law. The plaintiff and this court, however, notice that in *Empire Gas*, the court distinguishes the set of facts therein from a case in which a party "did not produce vitally important documents until the day of trial, and the responsible agent of the party was called to be cross-examined about his conduct and its relation to relevant admissible evidence." 646 F. Supp. at 274. That is what occurred during the trial of this case. There is no question that Mr. Weir and his firm were at all times agents of defendant CoreStates in this entire operation. The court permitted evidence that CoreStates withheld discovery especially of the "midnight hour" production of critical documents by Mr. Weir and the attempt to withhold T-15 which outlined the strategy to obstruct plaintiff and have Flatley pay all of CoreStates' counsel fees as well as indemnifying them for all damages including punitives. It was also relevant for the jury to be made aware in this case as to the cost to plaintiff of pursuing this litigation in the face of such obstruction.

5. Conspiracy evidence

By means of this ground for relief, CoreStates asserts that the court wrongly allowed "co-conspirator" hearsay evidence to be entered in the record contrary to Pa.R.E. 803(25)(E) where a conspiracy was neither pleaded nor proven.

CoreStates is correct in that no conspiracy was pleaded or proven. It points to three instances in which the issue arose. On the first occasion (*see* N.T. 6/6/00 pp. 27-32), the lawyer for CoreStates objected to Glenda Klein's statement that defendant Thomas Flatley told her that "the money was Pioneer's." At that time, counsel timely objected and an extensive colloquy on the basis of the objection followed. The court stated that "So far I haven't heard anything about it but basically it inures to the detriment of your defendant," but expressed the opinion that evidence of conspiracy was on the record, and hence statements of co-conspirators would be admitted under this theory. By this point in the trial, evidence that Mr. Flatley and agents of CoreStates had designed a plan to account for the setoff of Pioneer's funds within the context of the workout agreement was abundantly on the record. On the second occasion (N.T. 6/12/00 a.m. pp. 95-100), counsel interposed a pre-emptive objection to anticipated testimony by Gloria Sadler to her discussions with "people at American Financial." On this occasion, the court held that such statements would enter as "admissions." (*Id.* at 98.) On the third occasion (N.T. 6/27/00 a.m. pp. 61-66)[8] in which instance the court ruled against the defendants when they objected to "all of the hearsay . . . against CoreStates under this so-called conspiracy theory." The court ruled at pages 63-64 that the plaintiff had successfully proved a conspiracy.

Prior to the foregoing record citation the court had held the defendants' objection under advisement, admitting the testimony and determining whether or not to

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[8] Incorrectly cited in the defendant's brief as pp. 63-65.

instruct the jury to disregard the conspiracy-related hearsay. Ultimately, the court held that there was sufficient evidence on the record of a conspiracy so that statements of co-conspirators could be admitted pursuant to Pa.R.E. 803(25)(E).

The Pennsylvania cases permitting such "co-conspirator" evidence as an exception to the hearsay rule are largely criminal cases. They are effectively summarized in *Commonwealth v. Dreibelbis*, 493 Pa. 466, 475, 426 A.2d 1111, 1115 (1981), which remains good law in that it is cited by the commentators to the Pennsylvania Rules of Evidence. (*See* 802-803(25)(E) and Pennsylvania Bar Institute, Pennsylvania Rules of Evidence with Commentary 1998 p. 125.) In Dreibelbis the Supreme Court states: "This exception allows statements by a co-conspirator to be admitted against an accused if the statements are made during the conspiracy, [or] in furtherance thereof, and where there is in other evidence of the existence of a conspiracy. . . . The co-conspirator exception applies even where no party has been formally charged with conspiracy. *Commonwealth v. Stoltzfus*, 462 Pa. 43, 337 A.2d 873 (1975). Moreover, a conspiracy, for purposes of the co-conspirator exception to the hearsay rule may be inferentially established by showing the relation, conduct or circumstances of the parties, [citing] *Commonwealth v. Roux*, 465 Pa. 482, 350 A.2d 867 (1976)." 493 Pa. at 475, 426 A.2d at 1115 (citation omitted) (emphasis added) In that the Supreme Court does not distinguish between proof of the conspiracy for civil or criminal purposes as a predicate to admission of the hearsay statements, the defendants' plea for a new trial on this ground will be denied.

ARGUMENTS OF COUNSEL

The defendant bank has asked this court to grant it a new trial based on a finding that "The trial was unfair because of the improper conduct of Pioneer's counsel before the jury." In support of this plea, the defendant cites a collection of extremely argumentative statements by plaintiff's counsel which, if written down on paper, would qualify as neon-lit prose. The gist of plaintiff's counsel's comments, according to the defendant's analysis, was to push the actions in the very questionable conduct of the defendant's agents into a criminal, rather than civil, frame of reference.

The court has reviewed the statements of plaintiff's counsel and agrees with the defendant that at times the language plaintiff's counsel used, especially in his closing to the jury, may have crossed the line of advocacy and wandered into the land of the extreme. The court finds that the comments of counsel were an expression of his emotions and frustrations after spending $1.2 million of his client's money in the face of constant cheating and provocations on the part of CoreStates and its lawyers. The court does not find these expressions to be a calculated attempt to inflame or prejudice the jury. If these comments at all infected the jury-and neither this court nor any of the parties will ever have evidence that occurred-this court has already taken precaution against that development by granting the defendant's motion for remittitur. The size of the jury's punitive damage award is excessive, but as the court holds elsewhere in this opinion it is clearly not the result of unthinking passion or prejudice. The jury had before it an earnings statement of a multi-billion dollar corporation and acted in an attempt to punish and deter the corporation's behavior by depriving it

of less than one month's profits. However, as the defendant correctly points out, a new trial is only in order based upon counsel's statements if this court holds that the entire verdict was "obtained by incorrect statements or unfair argument or by an appeal to passion or prejudice . . . . " *Todd v. Lit Brothers*, 381 Pa. 109, 113, 112 A.2d 810, 812 (1955).

Since the court has otherwise held that the other, meaningful components of the jury's verdict are clearly based on the evidence and withstand re-examination in view of the record, the comments of plaintiff's counsel did not infect the jury's entire range of thought. What is more, it was not so much the definitional character of the words used by plaintiff's counsel that were objectionable but the descriptive nature of those words. For example, given the bank's fierce battle to keep the workout agreement out of the record, plaintiff's counsel had every reason, in fact, to use the word "cover-up" to address this conduct. (N.T. 6/5/00 a.m. pp. 50-51, 55.) By extension, then, counsel's comments, though extreme, were ultimately based upon the evidence contained within this exhaustive record. The court cannot reasonably find that counsel's statements were not based on the evidence and tended to influence the jury in resolving the issues before them "solely by an appeal to passion and prejudice . . . . " *Narciso v. Mauch Chunk Township*, 369 Pa. 549, 551, 87 A.2d 233, 234 (1952). It must also be emphasized that at all times this court instructed the jury to base its verdict upon the evidence that proceeded from the witness stand and not to allow their deliberations to be infiltrated by passion or prejudice.

The court finds, in sum, that (1) counsel's statements were extreme, and in the instances cited by the defendant

in its brief (*see* pp. 35-36 of defendant's brief), professionally out of bounds; and, however, (2) each and every statement cited had an ultimate reference to plaintiff's theory of recovery that was in turn grounded upon the facts of record. To the extent that any passion might have slipped into the jury's deliberations governing any aspect of the case, that result is cured by the remittitur herein-which brings the punitive damage picture into the realm of reason-and no new trial is warranted based upon counsel's statements alone.

CONSEQUENTIAL DAMAGES

1. The Award of Consequential Damages Was Proper

The jury awarded Pioneer $13.5 million in consequential damages, meaning that the jury accepted that Pioneer proved that greater damage to its business flowed from CoreStates' wrongful setoff of the loan package funds. CoreStates now asks for post-verdict relief on the grounds that consequential damages were neither properly pleaded nor sufficiently proven. The court will deny CoreStates' motion for a new trial and/or judgment n.o.v. on this ground as well.

(A) Were Consequential Damages Properly Pleaded?

The defendant and plaintiff both cite in their briefs recognized Pennsylvania practice manuals which hold in essence that so long as a defendant is reasonably placed on notice of the damages to which a plaintiff claims it is entitled then said damages will be submitted to the jury. (*See* 4 Stan. Pa. Prac. 2d § 21:63 (1993), and 2 Goodrich-Amram 2d § 1017(b):21). CoreStates further cites Pennsylvania law, specifically 1019(f) of the Pennsylvania Rules

of Civil Procedure and cases associated with it which hold that "Items of special damage shall be specifically stated." CoreStates notes that on the eve of trial, Pioneer "sought to slip a claim for consequential damages into its second amended complaint without notice to counsel and following a representation that the amendment would make no change relating to CoreStates." (*See* brief of defendant CoreStates p. 38 n.41.) The defendant further notes that this midnight claim by the plaintiff was subject to a motion to strike which was fully litigated by the parties. In examining the motion to strike, the court noted that the damages Pioneer suffered were subject to discovery and examination throughout the exhaustive period of litigation that preceded trial. Indeed, the Superior Court held in *Donlin v. J.J. Newberry Co.*, 319 Pa. Super. 310, 316, 466 A.2d 174, 177 (1983) that damages sought by the plaintiff were properly before the jury so long as the defendants had the means to discover them prior to trial. Furthermore, there is question in this court's mind whether the mandate of Rule 1019(f) applies to specific, i.e., liquidated damages rather than a business loss which a fact-finder would be free to calculate based upon contending evidence presented at trial-the situation in this case. While Pioneer's pleading of consequential damages may be said to be at best not in the most artful form, the court finds that no prejudice adhered to the defendants as a result. At least Pioneer's books were open and readable in the discovery process. By contrast, CoreStates' books were not as well paginated or public.

(B) Consequential Damages Were Recoverable in This Case

In tort actions in which business losses are demanded Pennsylvania law requires that the evidence presented

establish with reasonable certainty that they were proximately caused by the misconduct alleged. (*See Delahanty v. First Pennsylvania Bank N.A.*, 318 Pa. Super. 90, 120, 464 A.2d 1243, 1258 (1983). And that the damages must be a "proximate consequence of the breach, not merely remote or possible." (*See Dairyman's Co-Op Sales Assn. v. McCreary*, 132 Pa. Super. 524, 1 A.2d 508, 510 (1938).)[9]

Because the court has held that consequential damages could be proven and placed them before the jury with an instruction that the defendant does not question (except to disagree that there was causation), the jury's calculation of damages was not subject to the ordinary conversion formula, viz, that the measure of damages is the market value of the property converted plus interest. (*See Berry v. Heinel Motors Inc.*, 162 Pa. Super. 52, 58, 56 A.2d 374, 377 (1948).) Instead, the jury heard Pioneer's principals assert that as a result of the wrongful setoff and failure to explain the bank's conduct, Pioneer lost lines of credit from Nikko Financial Services Ltd. and Banc One. (*See* N.T. 7/10/00 p.m. pp. 70-74, 7/12/00 a.m. pp. 26-36 and 75-76.)[10]

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[9] The defendant also cites the federal case of *Advent Systems Ltd. v. Unisys Corp.*, 925 F.2d 670, 680 (3d Cir. 1991). While correctly reiterating Pennsylvania law governing the causation and recoverability of damages in the business context, the Advent Systems case stands for the proposition that damages for lost profits are not available to a new and untried business. Pioneer was not a new and untried business, despite the defendant's efforts to thus characterize it.

[10] Defendant CoreStates takes issue with the court's decision denying its objection to this testimony by Pioneer chairman Boaz Harel because Mr. Harel was not an expert. A glance at the Pennsylvania Rules of Evidence (*see* Rule 704) defining expert testimony should persuade the interpreter that Mr. Harel's testimony did not fall into the area of scientific knowledge or any other body of information which the

(Continued on following page)

The entire issue of whether Pioneer was entitled to recover consequential damages was fully and professionally litigated by the opposing parties. CoreStates, with the aid of its expert, Anthony Creamer, fully articulated its theory that Pioneer's business would have declined with or without the $1.7 million.[11] For its part, Pioneer's Boaz Harel, supported by Albert Nissin, demonstrated Pioneer's decline and satisfactorily related the plaintiff's loss of standing to occurrence of the setoff. Plaintiff also presented evidence from the Nikko concern that Pioneer lost an important credit opportunity in the amount of $200 million due to the plaintiff's inability fully to explain the loss of the settlement proceeds which were converted by CoreStates.

Moreover, a recitation of the whys and wherefores and the reasons for the jury's finding that CoreStates was

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jury would be incapable of analyzing without the intervention of a practiced or specialized mind.

[11] CoreStates complains that this court erroneously limited Mr. Creamer's testimony on what the court deemed to be ultimate issues. What concerned the court, as articulated on the record (N.T. 7/24/00 a.m. pp. 5-10), the portion of Mr. Creamer's testimony that the court excluded was his analysis of the events in the Nikko transaction, an interpretation that largely questioned the credibility of other witnesses. To the extent that Mr. Creamer did address ultimate issues it was within this court's discretion to admit or exclude his opinion depending on the helpfulness of the testimony versus its potential to cause confusion or prejudice. *See Kozak v. Struth*, 515 Pa. 554, 531 A.2d 420 (1987) and *Commonwealth v. Brown*, 408 Pa. Super. 246, 596 A.2d 840 (1991). Moreover, a review of Mr. Creamer's testimony would lead any reasonable interpreter to the conclusion that every empirical and opinionated point that this particular expert had to offer came across to the jury. As the plaintiff emphasizes in its brief, this court was exceedingly generous in permitting the defendant to present Mr. Creamer's testimony in that his role as an expert witness was revealed to all parties well beyond the deadline requiring such notice.

liable to Pioneer for consequential damages is unnecessary in this context. So long as the matter was before the jury, absent a showing that the evidence was willfully insufficient, this court will not disturb the jury's finding of consequential damages nor re-examine the amount, which the court finds is objectively based upon the record.

(C) The Measure of Damages

CoreStates also takes issue with the fact that this court permitted Pioneer to base its claim for consequential damages on the difference between its stock price on November 26, 1997, and its decline thereafter. CoreStates argues that "The more appropriate measure of the company's value was the book value of the business and the more appropriate measure of any consequential damages was the decline in book value after 1997-about $1.7 million to 1998 or $6.2 million to 1999." CoreStates also complains about the court's instruction (N.T. 7/26/00 p.m. p. 83) in which the court alludes to the capitalization and market value of the company on November 26, 1997. A review of the entire charge, however, shows that this court did not bind the jury's consequential damage calculations simply by using the term market value; that term encompasses both the method of damage calculation favored by the plaintiff and that favored by the defendant. The court expanded: "If you find that Pioneer plaintiff [sic] has established by a preponderance of the evidence that the destruction of the business was proximately caused by CoreStates' action and/or American Financial Corporation's action you must determine the damages expressed by the loss in value of plaintiff's business as a result of the conversion." (*Id.* at 84.) CoreStates takes issue with the use of the stock price as translated into market value as of

the date of the conversion and the coincident share price as a measure of damages. This court believes that the option to use the market price was put before the jury by the plaintiff, reiterated by the court in its instruction, but nowhere made binding upon the jury by virtue of its instruction. The jury was free to accept or reject this analysis. While it seems that the jury applied the $13.5 million market value figure in arriving at its assessment of consequential damages, it merely applied a permissible measure of damages.

PUNITIVE DAMAGES

I. Punitive Damages Will Be Remitted

"This will never do!"[12]

The court will grant the defendant's remittitur and reduce the amount of punitive damages awarded to $40,500,000, or three times consequential damages.

In reducing the award of punitive damages while upholding the fact of the punitive damage award, the court takes its guidance from the index of Pennsylvania appellate case law which addresses the issue of punitive damages. Under Pennsylvania law the standard for measuring the acceptability of punitive damages requires the court to determine whether the award falls within the range of fair and reasonable compensation or whether the punitive damage award so "shocks the sense of justice as to suggest that the jury was influenced by partiality, prejudice,

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[12] France's Jeffrey (later Lord Jeffrey of the Queen's Bench) beginning his essay on Wordsworth's "The Excursion" from Noyes, R., (Ed.) in English Romantic Poetry and Prose, p. 575, Oxford, 1956.

mistake, or corruption." *See Haines v. Raven Arms*, 536 Pa. 452, 455, 640 A.2d 367, 369 (1994) (citing *Carminati v. Philadelphia Transportation Co.*, 405 Pa. 500, 509, 176 A.2d 440, 445 (1962)). In *Haines*, the Supreme Court reduced an $8 million punitive damage award to $5 million in a case having to do with a 14-year-old plaintiff who sustained permanent injuries in an accidental shooting. In a supplemental opinion, the Supreme Court required that the trial court in reviewing punitive damages find first that a verdict shocks its conscience and set forth the conclusion and the reasons supporting a reduction of the verdict. *See Haines v. Raven Arms*, 539 Pa. 401, 403, 652 A.2d 1280, 1282 (1995).

In following the mandate of Haines, this court turns to *Kirbride v. Lisbon Contractors Inc.*, 521 Pa. 97, 102, 555 A.2d 800, 803 (1989), which sets forth the task of a jury in determining whether to award punitive damages and, if so, the amount.[13]

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[13] While Pennsylvania law does not require that a punitive damage award bear a proportional relationship to the award of compensatory damages (*see Kirkbride op. cit.* and *Delahanty v. First Pennsylvania Bank N.A.*, 318 Pa. Super. 90, 464 A.2d 1243 (1983)), this court specifically charged the jury that "the punitive damages must not totally be out of proportion to the damages suffered by the plaintiff." (N.T. 7/26/00 pp.86-87.) The court did so, mindful of the constitutional due process considerations that have played a role in the court's review of punitive damages awards. (*See BMW of North America Inc. v. Gore*, 517 U.S. 559, 575, 116 S.Ct. 1589, 1599 (1996) and *TXO Production Corp. v. Alliance Resources Corp.*, 509 U.S. 443, 482, 113 S.Ct. 2711, 2733 (1993), *see* especially, *TXO supra.*, at 481, 509 U.S. 113 S.Ct. at 2732 in which the court suggested a ratio of punitive damages to compensatory damages of 500 to 1 may "raise a suspicious judicial eyebrow." Also *see Pacific Mutual* at 23-24, 1046 in which the court states that a punitive damage award of four times the amount of compensatory damages did not "cross the line of constitutional impropriety.")

The Superior Court further instructs:

"[T]he court must look to the nature of the conduct engaged in by the defendant, the purpose that punitive damages are intended to achieve, the amount of the award and its likely effect as punishment for the defendant's outrageous conduct, as well as the relationship between the punitive and compensatory awards." *Sulecki v. Southeast National Bank*, 358 Pa. Super. 132, 138, 516 A.2d 1217, 1220 (1986) (citing *Feld v. Merriam*, 314 Pa. Super. 414, 434-38, 461 A.2d 225, 235-37 (1983), rev'd other grounds, 506 Pa. 383, 485 A.2d 742 (1984)).

Applying the foregoing analysis, the court in Sulecki reduced a punitive damage award of $75,000 to $35,000 in a case in which an automobile dealer had been defamed by a bank. *Id.* at 1220. The court held that a punitive damages award was appropriate in order to punish the bank for its conduct and to deter the bank from future similar conduct, but that $75,000 was not necessary to achieve those goals in that particular case.

This court's power to grant remittitur is subject to review for a clear abuse of discretion or error of law. *See Scaife Co. v. Rockwell-Standard Corp.*, 446 Pa. 280, 290, 285 A.2d 451, 456-57 (1971).

In all other respects, the jury's verdict in this case was not the result of passion or prejudice or haste. In arriving at a precise consequential damage award, the jury engaged in some very clear-headed arithmetic. The jury further was able to distinguish among the parties in terms of liability in finding no liability on the part of defendant Thomas Flatley.

The jury rendered a verdict on the question whether the account into which Pioneer's money was deposited was a general or special account. The foregoing are indicia of the jury's attention span. However, when it came to the award of punitive damages this jury did not follow this court's instruction as conscientiously and dispassionately as the court believes due process would require, only in terms of the amount awarded.

The amount awarded appears to transgress the defendant's due process rights under *TXO Production Corp. v. Alliance Resources Corp.*, 509 U.S. 443 (1993), in that it is "grossly out of proportion to the severity of the offense." 509 U.S. at 482. While the jury under the facts of this case had every reason to punish the defendant CoreStates having found essentially that the bank took what belonged to the plaintiff, refused to return it to the plaintiff when properly notified, and as a result drove the plaintiff's business into the ground, this court finds that the degree of punishment was excessive. Among other considerations, the $337 million punitive damage award would likely penalize innocent parties, namely depositors and borrowers who depend on the viability of the bank in order to feel insured of their own financial stability. It is sufficient under the circumstances of this case that CoreStates be required to pay an amount in punitive damages that makes it think twice before engaging in a setoff predicated on like circumstances.

The Supreme Court in *BMW v. Gore*, 577 U.S. 559 (1996) suggests that a court look to applicable legislative sanctions for comparable misconduct in arriving at a punitive damage award that is not violative of due process. 517 U.S. at 583. The Supreme Court has suggested that in

determining whether a punitive damage award is excessive, the court should "accord substantial deference to legislative judgments concerning appropriate sanctions for the conduct at issue." *See Browning-Ferris Industries of Vt. Inc. v. Kelco Disposal Inc.*, 492 U.S. 257, 301, 109 S.Ct. 2909, 2934 (1989).

Of course, there are no state statutes which punish errant conduct by banks. The only statute that approaches addressing the bank's conduct in the underlying case is the Pennsylvania Unfair Trade Practices and Consumer Protection Act, 73 P.S.A. § 201-9.2, which would award treble damages on a finding of unfair trade practices which victimized the consumer. In the business context, and on the federal level, the Sherman Antitrust Act, 15 U.S.C.A. § 1-7,15 also adopts the treble damage formulation for predatory business practices. And so, in fairness, this court will apply treble damages in reducing the amount of punitive damages irrationally awarded by this jury. Accordingly, the remittitur is granted and the plaintiff will be required to accept $40,500,000 in punitive damages or face a new trial on the issue of punitive damages.

II. AFMC is Not Entitled to Judgment as a Matter of Law on Count VII (Breach of Contract) Because the AFMC Loan Agreement Covered the Transfer of the First and Second Loan Portfolios

In evaluating a motion for judgment as a matter of law, the court reviews the record "and concludes that even with all factual inferences decided adverse to the movant the law nonetheless requires a verdict in his favor . . . . " *Campo v. St. Luke's Hospital*, 755 A.2d 20, 23 (Pa. Super. 2000), citing *Rohm & Haas Co. v. Continental Cas. Co.*,

732 A.2d 1236, 1247 (Pa. Super. 1999). According to this standard, AFMC cannot prevail on its motion.

The elements of a valid contract are "mutual assent and consideration." *Taylor v. Stanley Co. of America*, 305 Pa. 546, 551, 158 A. 157, 158 (1932). When attempting to determine the intent of the parties to a contract, "[I]t is their outward and objective manifestations of assent, as opposed to their undisclosed and subjective intentions, that matter." *Espenshade v. Espenshade*, 729 A.2d 1239, 1243 (Pa. Super. 1999), quoting *Ingrassia Construction Co. Inc. v. Walsh*, 337 Pa. Super. 58, 66, 486 A.2d 478, 483 (1984). According to the express terms of the loan and security agreement, AFMC agreed to repay all advances, including loans, forwarded by Pioneer pursuant to the agreement.

Although AFMC prefers to blame its refusal to honor the contract on the seizure by CoreStates, AFMC was still bound by the terms of the LSA. Its repeated refusal to repay the two loan portfolios to Pioneer constitutes a breach of the contract. Even if all factual inferences were decided in AFMC's favor, the defendant could not meet the standard set forth for a judgment as a matter of law.

Although the loans in question are clearly covered by the LSA, the extensive testimony of Pioneer's chief financial officer, Glenda Klein, served to further explain the LSA. The parol evidence rule prohibits a party from introducing evidence regarding the meaning of an agreement where the written agreement is clear and unambiguous on its face. *Sun Co. Inc. (R&M) v. Pennsylvania Turnpike Commission*, 708 A.2d 875, 878-79 (Pa. Commw. 1998). Specifically, parol evidence may not be used to

"vary, modify or supersede the written contract." *LeDonne v. Kessler*, 256 Pa. Super. 280, 287, 389 A.2d 1123, 1127 (1978). However, the parol evidence rule does not preclude evidence to either explain or clarify the reason for the agreement in the first place which was to keep RNG viable while AFMC decides whether or not it should rescue the beleaguered mortgage company from its financial woes.

During her testimony, Ms. Klein simply explained the loan portfolio transactions from their initiation through performance. Her testimony merely served to supplement what was already evidenced in both the LSA and the bailee letters, which were attached to both the first and second loan portfolios. Therefore, the parol evidence rule does not apply to Ms. Klein's testimony.

III. Thomas Flatley is Not Entitled to Judgment As a Matter of Law on Count II (Breach of Contract) Because AFMC Breached the Loan and Security Agreement with Pioneer and Mr. Flatley Was Personally Liable for Any Breach of That Agreement

As discussed above, AFMC clearly breached the LSA. According to the Flatley guaranty, Thomas Flatley was personally liable for any indebtedness or outstanding obligations of AFMC due Pioneer. (*See* exhibit T-12.) Since AFMC is liable for breach of contract, Mr. Flatley is also liable by extension of both the LSA and the Flatley guaranty. (*See* discussion, *supra* at I.) Thus, Mr. Flatley is not entitled to judgment as a matter of law.

IV. AFMC and Flatley Are Not Entitled to a New Trial on Counts II and VII (Breach of Contract) Because There Were No Errors Which Caused Prejudice to Either AFMC or Flatley

When considering a motion for a new trial, the court must first determine whether there were any mistakes made at trial and, if so, whether any of them provided a "sufficient basis" for granting a new trial. *Harman ex rel Harman v. Borah*, 562 Pa. 455, 756 A.2d 1116, 1122 (2000), citing *Spang & Co. v. U.S. Steel Corp.*, 519 Pa. 14, 24-25, 545 A.2d 861, 868 (1988).

The defendants first contend that the court improperly applied the standard for granting a directed verdict. A directed verdict may be granted "only where the facts are clear and there is no room for doubt." *Fetherolf v. Torosian*, 759 A.2d 391, 393 (Pa. Super. 2000), quoting *Lear Inc. v. Eddy*, 749 A.2d 971, 973 (Pa. Super. 2000). Furthermore, the trial court must "consider the facts in the light most favorable to the non-moving party and must accept as true all evidence which supports that party's contention and reject all adverse testimony." *Lear*, 749 A.2d at 973. The plaintiff clearly established at trial that both the loan and security agreement and the *Flatley* guaranty were valid contracts, and that both parties breached those contracts. The defendants offered no other evidence to dispute these claims, other than the fact that they blamed the entire dispute on CoreStates. Even when considering the facts in the light most favorable to AFMC and Flatley, and accepting as true all of their proffered evidence, neither defendant can prevail.

Neither were defendants prejudiced by the preclusion of Mr. Flatley's testimony. Upon cross-examination by Pioneer's counsel, Mr. Flatley repeatedly invoked his Fifth

Amendment rights against self-incrimination. (N.T. 6/14-6/15/2000.) It is clear that his testimony could not be outcome-determinative for either AFMC or Mr. Flatley himself if he refused to answer any questions. Thus, the court did not err in precluding his testimony.

Finally, the defendants attempt to argue impossibility of performance as a defense to the plaintiff's claim of conversion in a footnote. However, this argument lacks merit because it is clear that the misconduct of Flatley, and by implication AFMC, was the sole reason for the debit restraint which led to catastrophic results for all involved.

V. AFMC Is Not Entitled to Judgment As a Matter of Law on Count III (Conversion) Because AFMC Exercised Control Over Pioneer's Money and Agreed With CoreStates to Unreasonably Withhold Possession of the Money From Pioneer

Pursuant to the standard set forth for a judgment as a matter of law, AFMC cannot prevail. Even if all factual inferences were decided in favor of AFMC, Pennsylvania law does not support a favorable verdict for the defendant. The act of conversion includes "[a]cquiring possession of the goods, with an intent to assert a right to them which is in fact adverse to that of the owner [and] . . . [u]nreasonably withholding possession from one who has the right to it . . . . " *Norriton East Realty Corp. v. Central-Penn National Bank*, 435 Pa. 57, 60, 254 A.2d 637, 638 (1969), quoting Prosser, Torts, § 15 (2d edition 1955). Furthermore, the requisite intent does not necessarily have to be a matter of "conscious wrongdoing," but "an intent to exercise a dominion or control over the goods

which is in fact inconsistent with the plaintiff's rights." 435 Pa. at 60, 254 A.2d at 638-39, quoting Prosser at 70.

Although AFMC vehemently argued that it never exercised dominion or control over Pioneer's money, the agreement between AFMC and CoreStates, which is evidenced by exhibit T-15, suggests otherwise. Initially, AFMC recognized Pioneer's ownership rights in the funds; however, AFMC changed its position when it signed the letter agreement with CoreStates in March of 1998. (*See* exhibit T-15.) The evidence of AFMC's actions is sufficient to support a verdict of conversion. Although initially AFMC may not have intended to withhold the funds from Pioneer, it did eventually agree to withhold the funds from the plaintiff, to indemnify CoreStates from plaintiff's anticipated onslaught and to keep it secret.

VI. The Court Will Mold the Verdict Against Defendants American Financial Mortgage Company and Thomas Flatley to Include Reasonable Attorneys' Fees and Costs pursuant to the Express Language of Both the Loan and Security Agreement and the Flatley Guaranty

Absent either a written agreement or statutory provision, attorneys' fees are not recoverable in a cause of action. *Fina v. Fina*, 737 A.2d 760, 770 (Pa. Super. 1999), citing *Purdy v. Purdy*, 715 A.2d 473, 474 (Pa. Super. 1998). However, where the contract language is "clear and unambiguous" as to the amount of attorneys' fees recoverable, the provision must be enforced as written. *Id.* Paragraph 9.3 of the loan and security agreement between Pioneer and American Financial Mortgage Company (admitted as trial exhibit T-8) provides:

"Should lender [Pioneer] be required to enforce the provisions of this agreement or take or defend any legal action against or by borrower [AFMC] or any third party, then lender shall be entitled to payment of any and all costs and attorneys' fees, whether or not suit is actually commenced."

Since Pioneer was required to file a lawsuit and pursue litigation against AFMC, it is clear from this express language that due to AFMC's breach of its obligations, it is liable for all costs and attorneys' fees incurred by Pioneer.

In addition, paragraph 10 of the *Flatley* continuing guaranty (admitted as trial exhibit T-12) provides:

"Guarantor [Flatley] agrees to pay reasonable attorneys' fees and all other reasonable costs and out-of-pocket expenses which may be incurred by lender [Pioneer] in the enforcement of this guaranty or in any way arising out of, following, or consequential to the enforcement of borrower's [AFMC's] obligations, whether under this guaranty, the agreement, or otherwise."

Further, paragraph 1 of this document provides that Mr. Flatley is obligated to pay to Pioneer "any and all indebtedness and/or obligations of borrower [AFMC] to lender and the payment to lender of all sums which may be presently due and owing and of all sums which shall in the future become due and owing to lender from borrower under the [loan and security] agreement." It is clear that when Mr. Flatley signed this personal guaranty, he was exposing himself not only to the underlying liability, but also to the possibility of paying both attorneys' fees and costs, as evidenced by these two provisions. Therefore, both AFMC and Mr. Flatley are liable for attorneys' fees

and costs, pursuant to both the loan and security agreement and the *Flatley* continuing guaranty.

According to uncontested evidence presented at trial, $1.2 million in attorneys' fees were incurred during this litigation. In light of the circumstances surrounding this dispute, the court makes a finding that this amount is reasonable.

VII. The Court Will Mold the Verdict To Include Prejudgment Interest Against American Financial Mortgage Company, Thomas Flatley and CoreStates Because Such Interest Is Awardable As a Matter of Right in Breach of Contract Cases, and Prejudgment Interest Is Permissible in the Absence of a Contracted Rate Under Certain Circumstances

According to the Superior Court, "[i]n contract cases, prejudgment interest is awardable as [a matter] of right." *Daset Mining Corp. v. Industrial Fuels Corp.*, 326 Pa. Super. 14, 35, 473 A.2d 584, 595 (1984), citing *Eazor Express Inc. v. International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America*, 520 F.2d 951 (3d Cir. 1975), cert. denied; *Gold & Co. Inc. v. Northeast Theatre Corp.*, 281 Pa. Super. 69, 421 A.2d 1151 (1980). In addition, the right to such interest begins at the time payment is withheld after becoming due. *Palmgreen v. Palmer's Garage Inc.*, 383 Pa. 105, 108, 117 A.2d 721, 722 (1955). The express language of both the loan and security agreement and the *Flatley* continuing guaranty expressly provide for the interest due Pioneer for advances that were taken and not repaid.

Paragraph 2.3 of the loan and security agreement between Pioneer and AFMC states that:

"Each advance shall bear interest at lender's then applicable base rate (as hereinafter defined) plus two percentage points until the maturity date, and thereafter the interest rate on such advance shall increase by an additional three percent per annum until repaid. For purposes of this agreement, the "base rate" ("floating prime") shall be the Banc One, Texas prime rate at the time of the advance for loans secured by the mortgage loan and the documents upon which the advance is based."

According to the evidence, the Banc One prime rate in 1997 was 8.5 percent.

Payment in the amount of $1,779,519.99 was due Pioneer on the first and second loan portfolios on November 26, 1997, and the total interest due under the contract as of today is $890,442.56.

Because AFMC is liable for the interest pursuant to the loan and security agreement, Mr. Flatley is also liable for this amount pursuant to the *Flatley* continuing guaranty. (*See* discussion, *supra* at I.)

Although the action brought against CoreStates was not in contract but in tort, Pioneer is also entitled to prejudgment interest from the bank. According to the Superior Court, "the award of prejudgment interest [is] not only a legal right, but also . . . an equitable remedy awarded to an injured party at the discretion of the trial court." *Kaiser v. Old Republic Insurance Co.*, 741 A.2d 748, 755 (Pa. Super. 1999), quoting *Somerset Community Hospital v. Allan B. Mitchell & Associates Inc.*, 454 Pa. Super. 188, 201, 685 A.2d 141, 148 (1996); *Osborne v. Carmichaels Mining Machine Repair Inc.*, 427 Pa. Super. 159, 168-69, 628 A.2d 874, 879 (1993). Restitution in the form of prejudgment interest is necessary to avoid injustice and

compensate the plaintiff for the delay. *See* Restatement of Restitution, §§ 156, 157. In the absence of a contractual interest rate, interest is calculated as 6 percent from the date the payment is wrongly withheld. *See* generally, *Kessler v..Old Guard Mutual Insurance Company*, 391 Pa. Super. 175, 570 A.2d 569 (1990). Since the interest on the $1,779,519.99 in compensatory damages began to accrue at the time of the taking on November 26, 1997, the total currently stands at $78,854.29.

VIII. The Court Will Not Mold the Verdict to Find That American Financial's Settlement Account Was a Special Account Because the Court Will Not Overturn the Jury's Determination to the Contrary

A trial court may mold a verdict only to fit the clear intent and desires of the jury. *Mendralla v. Weaver Corp.*, 703 A.2d 480, 485 (Pa. Super. 1997); *Interstate Creamery Inc. v. Reinerth*, 212 Pa. Super. 335, 338, 243 A.2d 451, 452 (1968). When the court exercises its power to mold a verdict, it must not invade the province of the jury. 212 Pa. Super. at 338, 243 A.2d at 452; *Walsh v. Pennsylvania Gas & Water Co.*, 303 Pa. Super. 52, 57, 449 A.2d 573, 575 (1982). Upon hearing all of the evidence in this case and the appropriate charge by the court, the jury specifically determined that the settlement account was a general, not a special, account. (N.T. 6/30/2000 p.m. p. 76.) The jury clearly indicated their answer to the question of classification of the account. The court will not usurp the jury's function and mold the verdict in this way.

CONCLUSION

This court has denied all defendants' motions for judgment n.o.v., it has granted defendant CoreStates' motion for remittitur and ordered a reduction of punitive damages to $40,500,000.

Furthermore, the court has granted in part and denied in part plaintiff Pioneer Commercial Funding Corporation's motion for post-trial relief.

ORDER

And now, to wit, December 4, 2000, upon consideration of the motions for post-trial relief filed by defendants CoreStates Bank N.A. and First Union National Bank and all responses thereto and after argument thereon it is hereby ordered and decreed that with the exception of the grant of remittitur said motions are denied.

Judgment is entered in favor of plaintiff Pioneer Commercial Funding Corporation and against defendants CoreStates Bank N.A. and First Union National Bank as follows:

Compensatory damages in the amount of $1,779,-519.99 plus interest of $78,854.29.

Consequential damages in the amount of $13,500,000.

Punitive damages in the amount of $40,500,000.

Total judgment in favor of plaintiff Pioneer Commercial Funding Corporation and against defendants CoreStates Bank N.A. and First Union National Bank is $55,858,374.28.

It is further ordered and decreed, upon consideration of the motion for post-trial relief filed by defendants American Financial Mortgage Corporation and Thomas F. Flatley, and all responses thereto and after argument thereon, that said motion is denied.

It is further ordered and decreed, upon consideration of the motion for post-trial relief filed by plaintiff Pioneer Commercial Funding Corporation, and all responses thereto that said motion is granted in part and denied in part.

Judgment is entered in favor of plaintiff Pioneer Commercial Funding Corporation and against defendants American Financial Mortgage Corporation and Thomas F. Flatley as follows:

Compensatory damages on the contract and conversion claims in the amount of $1,779,519.99 plus interest of $890,442.56.

Attorneys' fees in the amount of $1,200,000.

Total judgment in favor of plaintiff Pioneer Commercial Funding Corporation and against defendants American Financial Mortgage Corporation and Thomas F. Flatley is $3,869,962.55.

[J-62-2004]
IN THE SUPREME COURT OF PENNSYLVANIA
EASTERN DISTRICT

PIONEER COMMERCIAL FUNDING CORP. AND BANK ONE, TEXAS, N.A.	:	No. 53 EAP 2003
v.	:	Appeal from the Order entered on 3/18/02 in Superior Court at No. 144 EDA 2001 affirming in part, reversing in part and remanding (Reargument denied on 5/21/02) the Judgment entered on 12/21/00 in the Court of Common Pleas, Civil Division of Philadelphia County at No. 885 April term 1998
AMERICAN FINANCIAL MORTGAGE CORP. AND THOMAS F. FLATLEY AND NORTHWEST FUNDING, INC. AND CORESTATES BANK, N.A.	:	
APPEAL OF: CORESTATES BANK, N.A.	:	

ORDER

PER CURIAM:

AND NOW, this 20th day of December, 2004, the application for reargument and associated requests for extensions of time to file *amicus* briefs are DENIED.

Madame Justice Newman did not participate in the consideration or decision of this case.

BAILEE LETTER FOR INVESTORS

PIONEER COMMERCIAL FUNDING CORP.

BANK ONE, TEXAS N.A.
1900 Pacific Ave.
Dallas, Texas 75201
Telephone: (212) 250-6082
Telecopy: (214) 290-6069

JOE SCHEUREN
AMERICAN FINANCIAL MORTGAGE CORPORATION
1150 FIRST AVENUE
SUITE 900
KING OF PRUSSIA PA 19406

The enclosed mortgage notes (see attached schedule) and other documents ("Collateral"), as more particularly described on the attached schedule, have been assigned and pledged to (a) Pioneer Commercial Funding Corp., ("Borrower") as collateral under a Loan and Security Agreement between Borrower and RNG MORTGAGE SERVICE, INC ("Originator), and (b) Bank One, Texas N.A., as Agent ("Agent") for itself and certain other Lenders ("Lenders"), a collateral under the Credit Agreement (as renewed, extended, amended, or re-stated, the "Credit Agreement") dated as of March 31, 1997, between Borrower Agent, and certain Lenders.

The Collateral is being delivered to you for purchase under an existing Take Out Commitment (as defined in the Credit Agreement). Either payment in full for the Collateral or the Collateral itself must be received by Agent within 45 days after the date of this letter. Unitl [sic] that time, you are deemed to be holding the Collateral in trust, subject to the security interests granted first to Borrower and then to Agent for Lenders and as Agent's bailee in

accordance with the applicable provisions of the Uniform Commercial Code. No property interest in the Collateral is transferred to you until Agent receives the greater of either (i) the agreed purchase price for $1,494,599.00 which is the full amount of the advance under the Credit Agreement in respect of the Collateral. If you receive conflicting instructions regarding the Collateral from Originator, Borrower, or Agent, you agree to act in accordance with Agent's instructions. AGENT RESERVES THE RIGHT, AT ANY TIME BEFORE IT RECIVES [sic] FULL PAYMENT, TO NOTIFY YOU AND REQUIRE THAT YOU RETURN THE COLLATERAL TO AGENT.

Payment for the Collateral must be made by wire transfer or immediately available funds to:

Bank One, Texas, N.A., Agent Account Number 1825160375
ABA Number 111000614 Attn: Gloria Sadler

Credit – Pioneer Commercial Funding Corp. TEL: (214) 290-6082
Settlement Account FAX (214) 290-6069
For Further Credit to:
RNG MORTGAGE SERVICE, INC

BY ACCEPTING THE COLLATERAL DELIVERED TO YOU WITH THIS LETTER, YOU CONSENT TO BE AGENT'S BAILEE ON THE TERMS DESCRIBED IN THIS LETTER. AGENT REQUESTS THAT YOU ACKNOWLEDGE RECEIPT OF THE ENCLOSED COLLATERAL AND THIS LETTER BY SIGNING AND RETURNING TO AGENT THE: ENCLOSED COPY OF THIS LETTER, BUT YOUR FAILURE TO DO SO DOES NOT NULLIFY YOUR CONSENT. If you fail to make full payment to Agent for it within 45 days after the date of

this letter, you are instructed to return all of the collateral to Agent. The preceding provision in no way affects or impairs any claim or cause of action against you in respect of your Take-Out Commitment.

This letter binds you and your sucessors, assigns, trustees, conservators, and receivers and inures to Agent, Lenders, and their respective successors and assigns.

Very Truly Yours, /s/ Glenda S. Klein

PIONEER COMMERCIAL FUNDING CORP.
Glenda S. Klein
SENIOR VICE PRESIDENT

BANK ONE, TEXAS, N.A., as Agent

By: /s/ Sarah Lee Murphy
Sarah Lee Murphy

ACKNOWLEDGED AND AGREED as of _____,199_
AMERICAN FINANCIAL MORTGAGE CORPORATION

By: _____

NAME: _____

TITLE: _____

NOTE RELEASE – REQUESTS

CTS – SYSTEM
RELX12 – MW.FNDPK

DATE: 10/27/97
PAGE: 1

CTS #	Name	Note Amount	Loan Number	Bank Code
0024501	CAMARENA, CARLOS	133538.00	1014743	BKO
0024502	MALDONADO, JUAN	142879.00	1014497	BKO
0024503	LAURIDSEN, RANDALL	139060.00	1014752	BKO
0024504	AGUILAR, LUIS	119376.00	1014715	BKO
0024507	GAONA/GONZALEZ/ GUERR	145120.00	1014666	BKO
0024511	SEPULVEDA, JACK	188700.00	1014499	BKO
0024617	MASON, CYNTHIA	86656.00	1014778	BKO
0024620	ACUNA, CAROLYN	66964.00	1014806	BKO
0024621	BRITO, PETE	113603.00	1014096	BKO
0024624	REDOLLEDO, LUIS R.	133293.00	1014647	BKO
0024625	COPELAND, BRIAN R.	142178.00	1014677	BKO
0024626	GAGER, ROBERT	83232.00	1014788	BKO

TIME: 16:32:31 AIRBILL #: F 0498610140
1494599.00 COMMITMENT# 12NORWEST

Acknowledged ----------

DEC. 12, 1997 DOC-NAME: 9072560-19971209
TIME: 10:34 AM

DATE : December 9, 1997
TO : DIST-KITE
FROM : DON MISHLER
SUBJECT: american financial kite

Walter Weir met with cb, bette and me this am to assist us in making a number of decisions on this account. We involved Jim Keenan of Loss Prevention in the discussion. Decisions Made: The State Street money that we trapped will be released to allow individuals to close on house purchases. The releases will coincide with the closing of the sale. The funds trapped in special purpose accounts where Am. Fin. Enterprises was collecting accounts receivable for others will be released except for any portion that may represent profit to AFE from their share of the collections. This release is important to protect the value of this company which is under an agreement of sale to close 12/19/97 for $1.6 mil. We made No decision to return $260,000 of Heller Financial money to the Daytona construction project account. Apparently, Am Fin used these funds to continue the kite in other accounts. Some of this

PF-Keys: 1-NEXT 2-RESET 3-ADD 6-DELETE 7-UP 8-DOWN 12-HELP
COMMAND:
TO: FROM: DATE:
NOTE:

132 MORE TEXT, PLEASE PRESS "ENTER" KEY.

DEC. 12, 1997 DOC-NAME: 9072560-19971209
TIME: 10:34 AM

Financial money to the Daytona construction project account. Apparently, Am Fin used these funds to continue the kite in other accounts. Some of this money got caught in the Am Fin Motg. acct when we discovered the kite. The project in Daytona is in jeopardy because of this situation and we may have to evaluate the potential for recovery from the project against this amount. On the $2 million trapped in an account that came here by wire from Norwest Bank, we have not determined a reason why it should be returned. This is a payment on a very convoluted transaction involving acompany in bankruptcy in California thatsold [sic] a portfolio of loans to Norwest. Go Figure how the funds got here. The total kite appears to be $4.9 mil. It will be decreased by the outcome of these situations. The company has promised us $1 mill [sic] from the sale of the collection business and the rest in one year, but it is clear that they have no visible means of doing so. Investigation continues. Walter and CB are leading the team. Paul Boston our favorite forensic account is out at the company and we have told Loss Prevention that they need to come to some conclusions on a variety of issues by the end of the week.

PF-Keys: 1-NEXT 2-RESET 3-ADD 6-DELETE 7-UP 8-DOWN 12-HELP
COMMAND:
TO: FROM: DATE:
NOTE:

132 MORE TEXT, PLEASE PRESS "ENTER" KEY.

LAW OFFICES OF

SAUL, EWING, REMICK & SAUL LLP

[Address And Phone Number Omitted In Printing]

November 25, 1997

Via Telecopier (215) 665-8464
Walter Weir, Jr., Esquire
Weir & Partners
100 South Broad Street
Suite 1200
Broad & Chestnut Streets
Philadelphia, PA 19110

Re: American Financial Mortgage Corporation
Account No. 14092-42683

Dear Walter:

On the dates listed below Norwest Bank wired to the above-referenced account the sums listed:

November 12, 1997	$1,454,699.80
November 13, 1997	209,984.33
November 19, 1997	114,835.86

These funds were for the release of security interests on mortgage loans being purchased by Norwest Bank. Pioneer Commercial Funding Corporation ("Pioneer") has advised us that the funds sent by the first wire should have been wired to Bank One, Texas, N.A. for credit to Pioneer.

Enclosed is a copy of a bailee letter from Pioneer, the holder of the security interest on the mortgage loans being sold to Norwest Bank. The letter directs the wire to be sent to Bank One for the account of Pioneer. This letter was sent to Norwest Bank by American Financial Mortgage Corporation. The original documents constituting the

loans being purchased, and which are referenced in the letter, were forwarded by Pioneer directly to Norwest.

On at least two separate occasions, on November 12 and November 17, Norwest Bank contacted CoreStates Bank stating that the wire was sent in error and sought to reverse the wire. Responding to CoreStates' inquiry, American Financial Mortgage Corporation on November 17, 1997 confirmed to CoreStates that the wire should be reversed. Subsequently, Norwest clerks erroneously sent two additional wires to the referenced American Financial account at CoreStates.

By this letter American Financial Mortgage Corporation again requests that all three wires be reversed to the account of Norwest Bank so that Norwest Bank can initiate the wire to the intended recipient of the wire, Pioneer Bank.

Very truly yours,

/s/ David R. Moffitt
David R. Moffitt

DRM/las
Enclosures